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No. 7820

United States
Circuit Court of Appeals

For the Ninth Circuit.

NORTH RIVER INSURANCE COMPANY,
a Corporation,
Appellant and Cross-Appellee,
vs.

GUY H. CLARK, as Receiver of the **MONT-**
BORNE LUMBER COMPANY, a Corpora-
tion,
Appellee and Cross-Appellant.


Transcript of Record

Upon Appeal and Cross-Appeal from the District Court of
the United States for the Western District of
Washington, Northern Division.

FILED

MAY 16 1935

PAUL P. O'BRIEN,
CLERK



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Washington, Northern Division.

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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ALFRED McBEE,

Everett, Washington. [1]*

*Page numbering appearing at the foot of page of original certified Transcript of Record.

In the Superior Court of the State of Washington
in and For the County of Skagit.

No. 13756

20512

GUY H. CLARK, as Receiver of the MONT-
BORNE LUMBER COMPANY, a corporation,
Plaintiff,

vs.

NORTH RIVER INSURANCE COMPANY, a
corporation,

Defendant.

COMPLAINT

Comes now the plaintiff, as receiver of the Montborne Lumber Company, a corporation, and complains and alleges as follows:

I.

That the above named defendant is a corporation, and during all of the times herein mentioned, was and now is transacting business in Skagit County, State of Washington.

II.

That heretofore and upon the 11th day of August, 1930, the Montborne Lumber Company was a corporation, organized and existed under and by virtue of the laws of the State of Washington, and that thereafter and to-wit, upon the 20th day of April, 1931, this plaintiff, by order of the Superior Court of the State of Washington for Skagit County, in

a certain cause therein pending wherein Roy Van Maren was plaintiff, and Montborne Lumber Company, a corporation, defendant, was appointed receiver of said defendant corporation, and that ever since said time, this plaintiff has been and now is the duly appointed, qualified and acting receiver of said corporation.

III.

That on said 11th day of August, 1930, the said defendant, in consideration of the sum of Six Hundred Thirty (\$630.00) Dollars premium, executed and delivered to these plaintiffs its certain policy of fire insurance, copy of which is hereto annexed, marked Exhibit "A" and made a part hereof. [2]

IV.

That on or about the 4th day of September, 1930, the locomotive mentioned and described in said policy, and while located upon the railroad owned by the assured, was damaged by fire and by collapse of bridges forming a part of said railroad, and resulting from such fire, to the amount of Fifteen Thousand (\$15,000.00) Dollars.

V.

That at said time and place, and while located upon the railroad of the assured and upon the branches and switches thereof, twelve (12) flat cars, covered by said policy, and owned by the Northern Pacific Railway Company, were by said fire and the collapse of bridges resulting therefrom,

as aforesaid, damaged to the amount of more than Eight Hundred Fifty (\$850.00) Dollars each, the amount of which damage is in excess of Ten Thousand Two Hundred (\$10,200.00) Dollars.

VI.

That at the times hereinbefore set forth the said flat cars were in the possession of the assured under an agreement wherein and whereby the said Assured undertook and agreed to return and deliver them to the Northern Pacific Railway Company in as good condition as when delivered to the assured, and that as a result of said damage to said cars the said assured has been and is now unable to return the same to the Northern Pacific Railway Company in as good condition as they were at the time of *deliver* to assured, or at all, and that by reason of said facts, assured is legally liable to said Northern Pacific Railway Company in excess of the sum of Eight Hundred Fifty (\$850.00) Dollars on account of each of said cars damaged as aforesaid.

VII.

That as soon as such loss was known to said assured, the same was reported to the defendant and that thereafter and on the 4th day of February, 1931, written proof of such loss was received by the said defendant by registered mail at its offices in San Francisco, California. [3]

VIII.

That by reason of the facts hereinbefore set forth, defendant is liable to plaintiff in the sum of Twenty Five Thousand Two Hundred (\$25,200.00) Dollars, with interest from the 4th day of February, 1931.

WHEREFORE, plaintiff demands judgment against the defendants in the sum of Twenty Five Thousand Two Hundred (\$25,200.00) Dollars, with interest as aforesaid, together with the costs and disbursements of this action.

AND FOR A FURTHER AND SECOND CAUSE OF ACTION. PLAINTIFFS ALLEGE the matters set forth in Paragraphs 1, *II and II* and further;

I.

That on or about the 30th day of August, 1930, the assured, Montborne Lumber Company, was in possession of five (5) certain freight cars belonging to the Northern Pacific Railway Company, which said freight cars assured *as* operating upon the line of its said logging railroad, and that under and by virtue of the terms of a contract between assured and said Northern Pacific Railway Company, assured was obligated to return the said cars to said railway company in as good condition as when the same were delivered to assured.

ii.

That on said 30th day of August, 1930, by reason of the derailment of the train in which said cars were being operated, the said cars were derailed, and were greatly damaged, and that by reason of such derailment, assured was compelled to spend the sum of Fourteen Hundred Seventy Six and 34/100 (\$1476.34) Dollars to repair said cars and

replace them upon said logging railroad, so that they might be returned to said Northern Pacific Railway Company.

III.

That the damage to each of said cars on account of the derailment as aforesaid, was as follows: [4]

Car No. 120753	\$272.56
Car No. 121528	247.84
Car No. 121012	347.89
Car No. 121969	316.87
Car No. 120539	291.18

IV.

That as soon as such loss was known to said assured, the same was reported to the defendant, and that thereafter and on the 4th day of February, 1931, written proof of such loss was received by the said defendant by registered mail at its offices in San Francisco, California.

WHEREFORE, plaintiffs demand judgment on their second cause of action in said sum of Fourteen Hundred Seventy Six and 34/100 (\$1476.34) Dollars, with interest from the 4th day of February, 1931, together with the costs and disbursements of this action.

For a further and third cause of action, plaintiff re-alleges paragraphs I, II and III of plaintiff's first cause of action, and further,

I.

That on or about the 30th day of August, 1930,

the assured, Montborne Lumber Company, was in possession of five certain freight cars belonging to the Northern Pacific Railway Company, which, other than those mentioned heretofore in this complaint, belonged to the Northern Pacific Railway Company, and which said freight cars the assured was operating upon its logging railroad and that under and by virtue of the terms of the contract between the assured and the said Northern Pacific Railway Company, the assured was obligated to return the said cars to said railway company in as good condition as when the same were delivered to assured.

II.

That on the 30th day of August, 1930, by reason of the derailment of the train in which the said cars were being operated, the said cars were derailed and were greatly damaged, and that thereafter, and to-wit, upon the 4th day of September, 1930, the said cars, while so derailed, were damaged and injured [5] by fire; that on account of the matters and things in this paragraph alleged, the said cars were damaged in the sum of \$850.00 each, or a total sum of \$4250.00.

III.

That as soon as such loss was known to said assured, the same was reported to the defendant, and that thereafter and on the 4th day of February, 1931, written proof of such loss was received by the said defendant by registered mail at its offices in San Francisco, California.

WHEREFORE plaintiff prays judgment against the defendant on his third cause of action in the sum of \$4250.00 with interest thereon from the 4th day of February, 1931, until paid, together with his costs and disbursements herein.

C. J. HENDERSON

Attorney for Plaintiff. [6]

(“EXHIBIT A”)

THE NORTH RIVER INSURANCE COMPANY
of THE CITY OF NEW YORK

Marine Department
Appleton & Cox, Inc., Attorney
No. 1 South Williams St.
New York

Incorporated 1822

Capital \$2,000,000

IN CONSIDERATION OF THE STIPULA-
TIONS HEREIN NAMED AND of SIX
HUNDRED THIRTY Dollars Premium
DOES INSURE MONTBORNE LUMBER
COMPANY

From the 8th day of August, 1930, at noon,
To the 8th day of August, 1931, at noon,
Standard Time at place of insurance against direct
loss or damage as hereinafter provided to an amount
not exceeding TWENTY FIVE THOUSAND
TWO HUNDRED DOLLARS, to Rolling Stock, as
per schedule, including all appliances, apparatus,

appurtenances, tools, spare and duplicate parts and equipment of every kind and description while on or attached to said Rolling Stock, while located as described herein, and not elsewhere.

1. Territorial Limits

This insurance covers only while the said Rolling Stock is in, on or about the Round House, Shops and Turntable of the assured or connecting lines and/or upon the line of any road owned or leased by the Assured, and its branches, spurs, side tracks and yards and upon such extensions or branches as may be constructed and/or leased by the Assured during the term of this policy and on the line of any connecting road or roads, all situated in the State of Washington, but it is warranted by the Assured to notify this Company, or the Agent who shall have issued the policy, in writing of their intention to use such extensions or branches as may be constructed and/or leased by the Assured prior to operation.

2. Perils Insured Against.

This policy Insures only:

Against loss or damage caused by fire, derailment or collision (coming together of cars and/or locomotives in shifting or coupling not to be considered a collision), collapse of bridges, lightning, cyclone, tornado and flood.

It is understood and agreed that in the event of loss or damage to any part or parts of the within insured property resulting from any one accident from perils insured against, this Company shall

only be liable for loss or damage in excess of Two Hundred Fifty Dollars (\$250.00)

3. Conditions.

(a) Notwithstanding anything in this policy to the contrary, it is warranted by the assured free from claim for loss or damage which may be attributed to, or *asire* from the act of any person acting or claiming to act under authority from any country or people, in a state of war (whether before or after declaration of war), revolution or internal commotion, and also from all consequences of hostilities, civil commotions, riots, and/or war-like operations, even if by lawless or unauthorized persons.

(b) It is expressly stipulated and made a condition of this contract that, in event of loss, this Company shall be liable [7] for no greater proportion thereof than the amount insured hereunder bears to NINETY per cent (90%) of the actual value of the property described herein at the time when such loss shall happen, nor for more than the proportion which this policy bears to the total insurance thereon.

(c) It is mutually understood and agreed that this Company shall not be liable beyond the actual cash value of the interest of the Assured in the property at the time of loss or damage not exceeding what it then cost the Assured to repair or replace the same with material of like kind and quality.

(d) In the event of any but a total loss under

this policy, the amount of said loss for which this policy is liable and shall be reinstated subject to all the conditions of the policy, the Assured warranting to pay pro rata premium upon the amount so reinstated from date of said loss.

(e) This entire policy shall be void if the Assured has concealed or misrepresented any material fact or circumstance concerning this insurance of the subject thereof; or in case of any fraud or false swearing by the Assured touching any matter relating to this insurance or the subject thereof, whether before or after a loss.

(f) It is warranted by the Assured that in case of loss or damage happening to the property insured hereunder, the same shall be reported as soon as the loss is known or expected to the Head Office of this Company at San Francisco, or to the Agent who shall have issued the policy. All adjusted claims shall be due and payable thirty days after presentation and acceptance of proofs of interest and loss at the office of this Company. No loss shall be paid hereunder if the Assured has collected the same from others.

(g) In the event of loss or damage caused by the risks and perils insured against, it shall be necessary for the Assured to use all lawful and proper efforts for the safeguard and recovery of the property or its value without prejudice to this insurance, and this Company will contribute to the just and reasonable charges thereof in such proportion as the sum named in this policy bears to the whole value at risk. And it is mutually agreed that

the acts of either party or their agents shall not be considered or held to be either a waiver or acceptance of an abandonment.

(h) No suit or action on this policy for the recovery of any claim shall be sustainable in any Court of Law or Equity unless the Assured shall have fully complied with all the foregoing requirements, nor unless commenced within twelve months next after the happening of the loss, provided that where such limitation of time is prohibited by the laws of the State wherein this policy is issued, then and in that event no suit or action under this policy shall be sustainable unless commenced within the shortest limitation permitted under the laws of such state.

(i) No person shall be deemed an Agent of this Company unless specifically authorized in writing by this Company.

(j) It is also agreed that no assignment or transfer hereof shall in any case relieve the assured of the property hereby insured from any or all of the conditions expressed in this policy, and that this policy shall be void in case of its being assigned or transferred without the written consent of this Company.

(k) This policy shall be cancelled at any time at the request of the Assured, or by this Company, by giving five (5) days written notice of such cancellation. If this policy shall be cancelled as hereinbefore provided, the premiums having been actually paid, the unearned portion shall be returned on surrender of the policy, this Company retaining

the customary short rate, it being mutually understood and agreed however, that a minimum earned premium of \$472.50 is guaranteed this Company, except that when this policy is cancelled by the Company by giving notice, it shall retain only the pro rata premium. [8]

(1) This insurance to be null and void to the extend of any other insurance specific or otherwise on the within described property which would attach and cover were it not for the fact of this insurance.

Provisions required by law to be stated in this Policy:: This policy is in a stock corporation, and is issued under and in pursuance of Section 130, 131 and 132 of the Insurance Law of the State of New York.

IN WITNESS WHEREOF, the undersigned on behalf of the said Company, have subscribed their named, in the City of New York.

This Policy is void unless countersigned by the authorized agent of this Company at San Francisco, Calif.

APPLETON & COX, INC.

Attorney, Douglas F. Cox, President.

Countersigned,

PACIFIC MARINE INSURANCE
AGENCY, INC.,

By S. S. HANSON, President

Date August 11, 1930

(Marine Dept.)

AMERICAN INSURANCE AGENCY

By F. A. FREDERICK

ENDORSEMENTS.

It is also understood and agreed that this policy covers the legal liability only of the assured on logging cars owned by others in the possession of the assured, but it is a warranty of this insurance that the insured shall not have at risk an average of more than twelve cars at a time.

It is further understood and agreed that loss, if any, on the first item (One Shay Locomotive #2703, 90 ton \$15,000.) is hereby made payable to the Pacific Equipment Company, Portland, Oregon, and the Montborne Lumber Company as their interests may appear.

All other terms and conditions remaining unchanged.

This slip is attached to and forms part of Policy No. 11187 of the North River Insurance Company issued to MONTBORNE LUMBER COMPANY.

Seattle, Wash., August 11, 1930.

(Marine Dept.)

AMERICAN INSURANCE AGENCY

By F. A. FREDERICK, Agent.

ENDORSEMENT

It is hereby understood and agreed that clause No 2 of the Policy to which this endorsement is attached is corrected to read as follows:

This policy insures only against direct loss or damage by fire, derailment or collision, collapse of bridges, lightning, cyclone, tornado and flood.

It is hereby agreed that the term "collision" as

used herein, is defined as including only contact with objects, moving or stationary on rails, ties, or roadbed, coming together of *card* and/or locomotives in shifting or coupling being always excepted, and excluding contact with any falling objects or any objects off the rails, ties or roadbed.

It is understood and agreed that in the event of loss or damage to any part or parts of the within insured property resulting from any one accident from perils insured against, \$250.00 shall be [9] deducted from any claim on locomotives, \$250.00 from any other piece of equipment valued at \$7,500.00 or over, \$50.00 from any other pieces of equipment valued at less than \$7,500.00, but not more than \$250.00 in any one accident.

All other claims and conditions remaining unchanged.

This slip is attached to and made a part of Policy No. 11187 issued to Montborne Lumber Company by the North River Insurance Company.

Dated at Seattle, Wash., August 11th, 1930.

(Marine Dept.)

AMERICAN INSURANCE AGENCY

By F. A. FREDERICK, Agent.

ENDORSEMENT

MONTBORNE LUMBER COMPANY

It is understood and agreed loss, if any hereunder, is payable to the Montborne Lumber Com-

pany and that the Pacific Equipment Company is no longer interested.

All other terms and conditions remaining unchanged.

This slip is attached to and forms part of Policy No. 11187 of the North River Insurance Company issued to Montborne Lumber Company, Seattle, Wash. August 14, 1930.

AMERICAN INSURANCE AGENCY

By F. A. FREDERICK, Agent

(Written on reverse side of policy)

				Amount of		
Trade Name	Year Built	Shop Number	Ton- nage	Insur- ance	Rate	Pre- mium
1 Shay loco- motive		#2703 90 Ton	\$15,000.00	2½%		\$375.00
12 CARS OWNED BY any others than the Assured, consisting principally of Northern Pacific flat cars, main line tanks, and coal gondolas, being an equal amount of cov- erage on each			\$10,200.00	2½%		\$255.00
Total			\$25,000.00			\$630.00

Filed May 28 1931, Will B. Ellis, County Clerk,
By Arthur Eliason, Deputy.

[Endorsed]: Filed Jun 19 1931. [10]

[Title of Court and Cause.]

PETITION.

COMES now the North River Insurance Company, defendant herein, and by this its petition respectfully shows to the court:—

That this is a civil action begun against your petitioner in this court and now pending therein, complaint and summons having been served on May 2, 1931.

The petitioner has not served or filed its answer or otherwise appeared in said cause, and the time for answering under the laws of the State of Washington will not expire until May 22, 1931.

When this action was commenced the plaintiff was and now is a citizen and resident of the State of Washington, and said Montborne Lumber Company was and now is a corporation organized and existing under and by virtue of the laws of the State of Washington, and the defendant then was and now is a corporation organized and existing under and by virtue of the laws of the State of New York.

The matter in dispute exceeds the sum or value of Three Thousand Dollars (\$3,000.00), exclusive of interest and costs.

The petitioner herewith submits to the court and files a bond as provided by the laws of the United States upon the removal of causes from a state court to the District Court of the United States, which bond is hereto attached.

WHEREFORE, your petitioner prays that this case be removed into the District Court of the United States for the Western District of Washington, Northern Division, and that this court accept this petition and said bond and proceed no further in the premises.

NORTH RIVER INSURANCE COMPANY

By: SAWYER and CLUFF

L. B. da PONTE and THOS H. MAGUIRE

Its Attorneys.

Office and Post Office Address:

909 Smith Tower,

Seattle, Wash.

(Verification omitted)

Filed May 21, 1931. Will B. Ellis, County Clerk.

[Endorsed]: Filed Jun 19, 1931. [11]

[Title of Court and Cause.]

NOTICE.

To GUY H. CLARK, as receiver of the Montborne Lumber Company, a corporation, plaintiff, and C. J. HENDERSON, his attorney;—

YOU ARE HEREBY NOTIFIED that on the 21st day of May, 1931, the defendant above named will file in the above entitled Court a petition and bond for removal of this cause to the District Court of the United States for the Western District of Washington, Northern Division, a copy of which

petition and bond are attached hereto and served herewith.

SAWYER AND CLUFF

L. B. da PONTE and THOS H. MAGUIRE

Attorneys for Defendant.

Received copy of the foregoing notice, also copies of petition and bond therein mentioned, this 19 day of May, 1931.

C. J. HENDERSON

Attorney for Plaintiff.

Filed May 21, 1931, Skagit County, Wash., Will B. Ellis, County Clerk, By Arthur Eliason, Deputy.

[Endorsed]: Filed Jun 19, 1931. [12]

[Title of Court and Cause.]

BOND ON REMOVAL.

KNOW ALL MEN BY THESE PRESENTS:—

That we, North River Insurance Company, a corporation organized and existing under and by virtue of the laws of the State of New York, as principal, and NATIONAL SURETY COMPANY, a corporation organized and existing under the laws of the State of New York, as surety, are held and firmly bound unto Guy H. Clark, as receiver of the Montborne Lumber Company, a corporation, in the penal sum of Five Hundred Dollars (\$500.00), lawful money of the United States for the payment of which well and truly to be made, we bind ourselves, our successors and assigns, jointly and severally firmly by these presents.

Sealed with our seals and dated the 16th day of May, 1931.

The condition of this obligation is such that the North River Insurance Company being about to file its petition to remove into the District Court of the United States a certain action brought by Guy H. Clark, as receiver of the Montborne Lumber Company, a corporation, plaintiff, against said North River Insurance Company, defendant, in the Superior Court of the state of Washington in and for the County of Skagit;

NOW, THEREFORE, if said defendant and petitioner shall enter in the District Court of the United States for the Western District of Washington, Northern Division, within thirty (30) days from the filing of said petition, a certified copy of the record in such action, and shall pay all costs that may be awarded by said District Court if said court shall hold that such action was wrongfully or improperly removed thereto, and shall there also appear and enter special bail in such action, if special bail was originally requisite therein, then this obligation to be void, otherwise to remain in full force and effect.

NORTH RIVER INSURANCE COMPANY

By: THOS. H. MAGUIRE

Its Attorney.

[Seal] NATIONAL SURETY COMPANY

By: R (illegible) WHYTE

Its Attorney-in-Fact.

Filed May 21, 1931, Skagit County, Wash., Will B. Ellis, County Clerk, By Arthur Eliason, Deputy.

[Endorsed]: Filed June 19, 1931. [13]

[Title of Court and Cause.]

ORDER

The above named defendant having filed its petition and bond for removal of this action to the District Court of the United States for the Western District of Washington, Northern Division and presented the same to this court, now on motion of the said defendant,

IT IS ORDERED that said petition and bond be accepted and that this court proceed no further in this cause.

DONE IN OPEN COURT this 21st day of May, 1931.

GEO. A. JOINER, Judge.

Filed May 21, 1931, Skagit County, Wash., Will B. Ellis, County Clerk, By Arthur Eliason, Deputy.

[Endorsed]: Filed Jun 19, 1931. [14]

[Title of Court and Cause.]

ANSWER.

COMES now the defendant, and answers plaintiff's complaint as follows:

I.

Admits Paragraph I.

II.

Admits Paragraph II.

III.

Answering Paragraph III, admits that on August 11, 1930, the defendant, in consideration of the payment of Six Hundred Thirty Dollars (\$630.00) premium, executed and delivered to the Montborne Lumber Company a policy of insurance, and that Exhibit "A" attached to the complaint is a substantially correct copy of said policy, and except as herein expressly admitted, denies said Paragraph III and the whole thereof.

IV.

Answering Paragraph IV, defendant denies that the locomotive mentioned and described in said policy was on September 4, 1930, or at any other time, damaged by fire or by collapse of bridges in the amount of Fifteen Thousand Dollars (\$15,000) or any sum whatsoever.

V.

Answering Paragraph V, defendant admits that on or about September 4, 1930, there were in assured's possession twelve (12) flat cars owned by the Northern Pacific Railway Company, which cars were damaged by fire, but defendant denies knowledge or information as to the full extent of such damage sufficient to form a belief thereof, and therefore denies that said cars were damaged to the amount of Eight Hundred Fifty Dollars (\$850.00) each, or any part thereof, and otherwise, except as herein admitted, denies said Paragraph V and the whole thereof. [15]

VI.

Answering Paragraph VI, defendant admits that following said fire the assured was unable to return said flat cars to the Northern Pacific Railway Company, but otherwise denies said Paragraph VI and the whole thereof, and particularly denies that assured is legally liable to said Northern Pacific Railway Company in the sum of Eight Hundred Fifty Dollars (\$850.00) or any sum whatsoever, on account of each of said cars or any of them.

VII.

Answering Paragraph VII, defendant admits that defendant received on or about February 4, 1931, a writing designated by assured as "proof of loss", but except as herein expressly admitted, denies said Paragraph VII and the whole thereof.

VIII.

Answering Paragraph VIII, defendant denies that it is liable to plaintiff or to any other person, firm or corporation under said policy, in the sum of Twenty-five Thousand Two Hundred Dollars (\$25,200), with interest, or in any sum whatsoever.

And defendant answers plaintiff's second cause of action as follows:—

I.

Answering Paragraph I, defendant admits that on or about August 30, 1930, there were in assured's

possession five (5) flat cars owned by the Northern Pacific Railway Company, but otherwise denies said Paragraph I and the whole thereof.

II.

Answering Paragraph II, defendant admits that on or about August 30, 1930, said five (5) cars were derailed, but denies that assured was compelled to spend or has spent One Thousand Four Hundred Seventy-six and 34/100 Dollars (\$1,476.34) or any sum whatsoever, to repair said cars or replace them on the track, and otherwise denies all of Paragraph II, except as herein admitted.

III.

Answering Paragraph III, defendant denies that said cars or any of them were damaged in the sums therein set forth, except that defendant admits that the Northern Pacific Railway Company expended the sum of Four Hundred Eighty-two and 13/100 Dollars (\$482.13) to repair said cars.

IV.

Defendant denies each and every allegation set forth in Paragraph IV and the whole thereof.

And defendant answers plaintiff's third cause of action as follows:—

I.

Answering Paragraph I, defendant admits that on or about August 30, 1930, the assured was in

possession of five (5) flat cars belonging to the Northern Pacific Railway Company, but otherwise denies said Paragraph I and the whole thereof.

II.

Answering Paragraph II, admits that on September 4, 1930, said cars were damaged by fire, but denies knowledge or information of the full extent of such damage sufficient to form a belief thereof, and therefore denies that said cars were damaged in the sum of Eight Hundred Fifty Dollars (\$850) each or any part thereof, and otherwise, except as herein admitted, denies said Paragraph II and the whole thereof.

III.

Denies Paragraph III and the whole thereof.

AND FOR FURTHER ANSWER, and by way of affirmative defense, defendant alleges as follows:

I.

That on September 4, 1930, the Montborne Lumber Company had in its possession the twelve (12) flat cars described in plaintiff's first cause of action, and the five (5) cars mentioned in plaintiff's third cause of action, all of which said cars were the property of the Northern Pacific Railway Company. On said date said cars were all damaged by a forest fire in the vicinity of the Montborne Lumber Company's tracks.

That on August 30, 1930, said Montborne Lumber

Company had in its possession the five (5) cars mentioned in plaintiff's second cause of action, which cars were the property of [17] the Northern Pacific Railway Company and were derailed. Following the return of said cars to the Northern Pacific Railway Company, said Railway Company expended the sum of Four Hundred Eighty-two and 13/100 Dollars (\$482.13), in repairing same.

II.

That the full damage to all of said cars did not exceed the sum of Eight Thousand Dollars (\$8,000), and on March 11, 1931, defendant paid to the Northern Pacific Railway Company the sum of Eight Thousand Dollars (\$8,000) in full settlement and satisfaction of any and all claims said Railway Company might have on account of the damage to or destruction or loss of any and all cars of said Railway Company covered by said policy of insurance.

III.

That after the payment of said sum of Eight Thousand Dollars (\$8,000), and on or about the 7th day of December, 1931, said Northern Pacific Railway Company duly served upon plaintiff and filed with the Clerk of the Superior Court of the State of Washington in and for Skagit County, a claim in that cause entitled "Roy Van Maren, Plaintiff, v. Montborne Lumber Company, a corporation, De-

fendant, No. 13524", in which claim said Northern Pacific Railway Company stated that it neither had nor made any claim against said Montborne Lumber Company or its Receiver on account of damage to or failure to return the cars set forth in plaintiff's first, second and third causes of action, and released and discharged said Montborne Lumber Company and its Receiver from any and all liability for or on account of damage to said cars or failure to return the same, pursuant to the interchange contract in effect between said Railway Company and said Lumber Company, or otherwise.

IV.

That by reason of said payment of Eight Thousand Dollars (\$8,000.00) and the release of liability mentioned in Paragraph III hereof, the liability of the Montborne Lumber Company and its Receiver to said Northern Pacific Railway Company and the liability of defendant to said Montborne Lumber Company or its [18] Receiver, under the terms of said policy of insurance, were entirely extinguished.

V.

That said Montborne Lumber Company as a result of said fire and said derailment, suffered no damage or injury for which it was entitled to recover from this defendant under said policy of insurance.

WHEREFORE, defendant prays judgment that

plaintiff recover nothing herein, and for its costs and disbursements herein incurred.

SAWYER and CLUFF

L. B. da PONTE

THOS. H. MAGUIRE

Attorneys for Defendant.

(Verification omitted)

Received a copy of the foregoing Answer this 29 day of January, 1932.

C. J. HENDERSON

Attorneys for Plaintiff.

[Endorsed]: Filed Feb. 1, 1932. [19]

[Title of Court and Cause.]

REPLY.

Comes now the plaintiff, and replying to the answer of the defendant, admits, denies and alleges as follows:

I.

Replying to the answer to plaintiff's first cause of action, the plaintiff herein denies each and every allegation therein contained except insofar as the same may be consistent with the matters and things alleged in plaintiff's first cause of action in the complaint herein.

Replying to the answer to plaintiff's second cause of action, the plaintiff herein denies each and every allegation therein contained except insofar as the

same may be consistent with the matters and things alleged in plaintiff's second cause of action in the complaint herein.

Replying to the answer to plaintiff's third cause of action, the plaintiff herein denies each and every allegation therein contained except insofar as the same may be consistent with the matters and things alleged in plaintiff's third cause of action in the complaint herein.

I.

Replying to paragraph I of the affirmative defense in said answer contained, the plaintiff herein denies each and every allegation therein contained except insofar as the same may be consistent with the matters and things alleged in plaintiff's complaint.

II.

Replying to paragraph II of said affirmative defense, the plaintiff denies each and every allegation therein contained, except insofar as the same may be consistent with the matters and things alleged in plaintiff's complaint. [20]

III.

Replying to paragraph III of said affirmative defense, the plaintiff denies each and every allegation therein contained, except insofar as the same may be consistent with the matters and things alleged in plaintiff's complaint.

IV.

Replying to paragraph IV of said affirmative defense, the plaintiff denies each and every allegation therein contained, except insofar as the same may be consistent with the matters and things in plaintiff's complaint alleged.

V.

Replying to paragraph V of said affirmative defense, the plaintiff denies each and every allegation therein contained, except insofar as the same may be consistent with the matters and things alleged in plaintiff's complaint.

C. J. HENDERSON

Attorney for Plaintiff.

State of Washington

County of Skagit—ss.

Guy H. Clark, being first duly sworn, on oath deposes and says:

That he is the plaintiff named in the within and foregoing Reply, that he has read the same, knows the contents thereof and that the same is true as affiant verily believes.

GUY H. CLARK

Subscribed and sworn to before me this 29th day of August, 1932.

ALFRED McBEE

Notary Public in and for the State of Washington, residing at Mount Vernon.

[Endorsed]: Filed Feb. 8, 1933. [21]

In the District Court of the United States for the
Western District of Washington,
Northern Division.

No. 20512

GUY H. CLARK, as Receiver of the Montborne
Lumber Company, a corporation,

Plaintiff,

vs.

NORTH RIVER INSURANCE COMPANY, a
corporation,

Defendant.

JUDGMENT.

This matter regularly coming on to be heard upon application for entry of judgment herein, this cause having been tried to the court without a jury on October 3, 1934, upon stipulations of facts dated May 1, 1934, and October 3, 1934, and the court heretofore, to-wit, on October 20, 1934, entered and filed its memorandum decision herein, and the court having made and entered findings of fact and conclusions of law this 14 day of January, 1935, plaintiff appearing by his counsel, C. J. Henderson and Alfred McBee, and defendant appearing by its counsel, Sawyer & Cluff, L. B. DaPonte and Robert S. Macfarlane, and the court being fully advised in the premises;

NOW, THEREFORE, it is

ORDERED, ADJUDGED and DECREED that the plaintiff have and recover of and from the defendant Seven Thousand Dollars (\$7,000.00), to-

gether with interest at the rate of six per cent (6%) from date hereof, together with costs and disbursements as provided by law.

Exceptions allowed both plaintiff and defendant.

DONE IN OPEN COURT THIS 14 day of January, 1935.

JOHN C. BOWEN

District Judge.

Presented by:

ROBERT S. MACFARLANE

Notice of presentation waived.

C. J. HENDERSON

ALFRED McBEE

Attys for Pltf.

[Endorsed]: Filed Jan 14 1935. [22]

[Title of Court and Cause.]

BILL OF EXCEPTIONS.

BE IT REMEMBERED: That this cause came on for trial on the 3rd day of October, 1934, in the above-entitled Court before the Honorable John C. Bowen, Judge thereof, and that thereafter the following proceedings were had, that is to say:

Plaintiff appeared by Messrs. C. J. Henderson and Alfred McBee, his attorneys, and the defendant appeared by Messrs. Sawyer & Cluff, represented by Harold M. Sawyer, Esq. and L. B. da Ponte and Robert S. Macfarlane, its attorneys.

It further appeared that all of the facts were incorporated in written stipulations filed in the above-entitled cause on the 1st day of May, 1934, and the 3rd day of October, 1934. The written stipulation filed on the 1st day of May, 1934, was and is in words and figures as follows, that is to say: [23]

[Title of Court and Cause.]

STIPULATION

IT IS HEREBY STIPULATED by and between the parties hereto, by their respective counsel as follows:—

(1) That this stipulation shall constitute a stipulation as to the facts in the above entitled cause, and that the said cause shall be tried to the court without a jury.

(2) That on or about August 11, 1930, a policy of insurance was effected by the Montborne Lumber Company, (hereinafter called Lumber Company), with the defendant, the original of which policy of insurance is in the possession of plaintiff, and will be produced at the time of trial and admitted in evidence.

(3) That the lumber company at all times here in question was engaged in the business of logging near Montborne, Skagit County, Washington, and in connection with said operations said lumber company built a logging railroad back into the timber to the scene of its logging operations from the station of Montborne on the Seattle-Sumas main line of the Northern Pacific Railway Company.

(4) That on or about September 4, 1930, a forest fire broke out in the holdings of the Lumber Company and spread onto and over portions of the logging railroad owned and [24] operated by the Lumber Company, destroying certain bridges and trestles of said logging railroad.

(5) That the Lumber Company owned a certain 90-ton Shay locomotive, shop No. 2703, which locomotive at the time of the fire heretofore mentioned was situated on the logging railroad in the woods; and that by reason of the aforementioned destruction of certain bridges and trestles on the logging railroad between the locomotive and Montborne station, the said locomotive was marooned. The locomotive itself was never in contact with the fire and sustained no physical damage as a result of the fire. The cost of sufficiently repairing the said bridges and trestles in order to get the locomotive out of the woods and down to Montborne station would exceed the value of the locomotive. That at the time of the fire in question the reasonable market value of the said locomotive was \$7,000.00.

(6) That the Northern Pacific Railway Company (hereinafter called the Railway Company), is a corporation engaged in business as a common carrier railroad, and carries on its business in Skagit County and in the State of Washington and elsewhere. That the said Railway Company and the Lumber Company entered into a certain interchange agreement dated December 19, 1927, attached hereto and marked Exhibit 1 and made a part hereof as fully as if set forth herein in full, which said inter-

change agreement fully sets forth the rights and liabilities of the Lumber Company and the Railway Company with respect to cars and equipment belonging to the Railway Company used by the Lumber Company, which said agreement was in full force and effect at all times material to this litigation. [25]

(7) That on August 11, 1930, and for a long time prior thereto, and until the time of the fire before mentioned, the Railway Company furnished the Lumber Company its flat cars, main line tanks and coal gondolas for the purpose of loading and/or unloading freight under said interchange agreement; that the Lumber Company did not own any logging flat cars, main line tanks or coal gondolas, and that all rolling equipment of said character used or intended to be used at any time material to this litigation upon the logging railroad of the Lumber Company was rolling equipment owned by the Railway Company and furnished pursuant to the said interchange agreement.

(8) That it was the practice and procedure of both parties under the interchange agreement for the Railway Company to deliver empty logging flat cars to the Lumber Company upon the siding at Montborne station; that thereafter the Lumber Company, with its own locomotive, took said logging flat cars from said siding over its logging railroad into the timber to the scene of its operations for the purpose of loading; that after loading, the logging flat cars were thereupon taken by the

locomotive of the Lumber Company back to the siding at Montborne station, from which siding said cars were picked up by the Railway Company for further transportation over its railroad to destination.

(9) That this practice and procedure and this form of interchange agreement, with substantially identical provisions, was usual and customary between logging railroads and common carrier railroads in Western Washington at all times material to this litigation.

(10) That on or about August 30, 1930, five certain logging flat cars, (N.P. 120753, N. P. 121-526, N. P. 121012, [26] N. P. 121969, N. P. 120-539), belonging to the Railway Company and in the possession of the Lumber Company pursuant to the terms of the interchange agreement, were derailed, and that by reason of said derailment were damaged in the amount of \$482.13, which damage was fully repaired by the Railway Company at its expense.

(11) That on or about September 4, 1930, said cars which had been derailed and repaired, together with other logging flat cars, (N. P. 120107, N. P. 121134, N. P. 122087, N. P. 121041, N. P. 121683, N. P. 120411, N. P. 121116, N. P. 120880, N. P. 121447, N. P. 121818, N. P. 120565, N. P. 121275, N. P. 121379, N. P. 121385, N. P. 122011, N. P. 121742 and N. P. 119222), totalling 22 logging flat cars, were destroyed by the forest fire heretofore mentioned, which said logging flat cars were the

property of the Railway Company, and were in the possession of the Lumber Company pursuant to the terms of the interchange agreement heretofore mentioned.

(12) That no flat cars, main line tanks or coal gondolas other than those herein described belonging to others than the Lumber Company were upon the logging railroad or in the possession of the Lumber Company at the time of the fire.

(13) That the loss and damage caused by derailment and/or fire to all of said cars was in the total sum of \$8,000.00.

(14) That shortly after the said fire said Lumber Company became hopelessly insolvent and went into receivership and plaintiff is now the receiver of said Lumber Company, liquidating the same.

(15) That on or about January 20, 1931, there was filed in the proper proceeding involving the insolvency [27] and receivership of the Lumber Company, a claim by the Northern Pacific Railway Company against the Lumber Company, which said claim is attached hereto marked **Exhibit 2**, and made a part hereof the same as if herein fully set out; that the detailed statement and vouchers referred to in Paragraph 2 of said claim, refer to demurrage and other items not material to the present litigation, and are therefore, by agreement, eliminated from the said exhibit.

(16) That on or about November 28, 1931, there was properly and timely filed in the proper proceed-

ing involving the insolvency and receivership of the Lumber Company, a waiver and release of the claims of the Railway Company against the Lumber Company on account of any legal liability or otherwise for damage to any of said logging flat cars for any cause whatsoever, all as appears in the so-called "amended claim of the Northern Pacific Railway Company" attached hereto and marked Exhibit 3, and made a part hereof the same as if herein fully set out; that the cars itemized and listed in said amended claim are the cars damaged by derailment and fire as heretofore described herein; that the amounts claimed as shown in the last two paragraphs of said amended claim are in addition to all loss or damage on account of the said logging flat cars; that said items are immaterial to this litigation and refer to demurrage and other like charges.

(17) That the defendant Insurance Company paid to the Railway Company on February 26, 1931, the sum of \$8,000.00 in full settlement and satisfaction of any and all claims said Railway Company might have against it or the Lumber Company or on account of the damage to or destruction or loss of any and all cars of said Railway Company covered by the said policy of insurance; that [28] said settlement and satisfaction made by the defendant Insurance Company was without the consent of the receiver.

(18) By reason of all of the foregoing, the defendant Insurance Company has refused to pay or

recognize the claim of the Lumber Company now being prosecuted seeking \$7,000.00, because of the aforesaid Shay locomotive and \$8,000.00 because of the derailment and burning of the aforesaid logging flat cars.

(19) In the event this court should decide either or both phases of this case in favor of the plaintiff, it is agreed that judgment is to be entered in the applicable amount or amounts herein set forth as the loss or damage, said judgment to carry interest from its date.

(20) That this stipulation is to be read in connection with the pleadings herein.

Dated this 1st day of May, 1934.

C. J. HENDERSON

and ALFRED McBEE

Attorneys for Plaintiff.

SAWYER & CLUFF

L. B. da PONTE and

ROBERT S. MACFARLANE

Attorneys for Defendant.

EXHIBIT 1.

CONTRACT made this 19th day of December, A.D. 1927, between the NORTHERN PACIFIC RAILWAY COMPANY, a Wisconsin corporation, hereinafter called "Railroad" and the Montborne Lumber Company, a Washington corporation, hereinafter called "Lumber Company."

In consideration of the mutual dependent promises stated in this contract the parties agree:—

I.

Connections between the tracks of the parties hereto [29] have been installed at Montborne, Washington, under the provisions of a contract between them dated November 22, 1926, and the parties agree to interchange carload business at such point through such connections.

II.

The Lumber Company agrees to pay the Railroad for all damage which cars delivered to it by the Railroad through such connections may sustain from any cause whatever while in its possession and to indemnify and protect the Railroad against any claim for personal injury or death on account of alleged defects in such equipment and to return promptly all cars received from the Railroad and be governed by tariff provisions relating to demurrage.

GTR FRB WEC JEC AVB FEW

III.

For the purpose of fixing liability for loss and damage to cars and their loads, cars and loads placed by the Railroad at the point of interchange for movement over the logging railroad of the Lumber Company or for the use of the Lumber Company shall be deemed to be in the Lumber Company's possession and to continue in its possession until the Railroad shall move said cars from said point of interchange on to its own main track.

IN WITNESS WHEREOF the parties hereto have caused this contract to be executed by officers

thereunto duly authorized on the day and year first above written.

NORTHERN PACIFIC RAILWAY
COMPANY

By F. F. WILLIAMSON

Its Vice President

WITNESSES:

T. K. YOUNG

R. D. VanVOORHIS

MONTBORNE LUMBER COMPANY

By THOMAS SMITH

Its President.

WITNESSES:

FRANK F. DAY

L. G. HARVEY

EXHIBIT 2.

In the Superior Court of the State of Washington
in and for Skagit County.

No. 13524

ROY VAN MAREN,

Plaintiff,

vs.

MONTBORNE LUMBER COMPANY, a corpora-
tion,

Defendant.

CLAIM OF NORTHERN PACIFIC RAILWAY
COMPANY. [30]

Pursuant to the court's order and the notice of

receivers dated the 21st day of October, 1930, that claims duly verified with proper vouchers attached be presented on or before January 24, 1931, the Northern Pacific Railway Company states the following:—

There is attached hereto a statement in detail with vouchers attached showing an amount of \$6,177.40 due from the Montborne Lumber Company to Northern Pacific Railway Company on account of the items shown in the detailed statement and vouchers attached hereto, and said details and vouchers are self-explanatory.

In addition to said amount, the Montborne Lumber Company has in its possession 20 cars belonging to the Northern Pacific Railway Company delivered by claimant to said Montborne Lumber Company under the interchange contract dated the 19th day of December, 1927, copy of which is in the possession of the Montborne Lumber Company. Said cars have been more or less damaged, as shown by the statement hereto attached. Claimant states that there is a policy of insurance on said cars, or some of them, issued to Montborne Lumber Company by the North River Insurance Company, and this company claims that said policy inures to its benefit and that it is entitled to the protection of said policy on said cars and to the money due thereon. Claimant has not received any sum on account of said insurance and cannot state when it will receive anything thereon, nor the amount thereof, and therefore cannot at this time state

what balance will be due from the Montborne Lumber Company and its receivers on account of the damage or destruction of said cars. Claimant further shows that there will be salvage from said cars, which should be deducted from said account, but cannot state [31] at this time what the amount of said salvage will be, nor the cost of recovering said cars. Claimant will file an amended claim at a later date showing the balance due from the Montborne Lumber Company on account of said cars after deducting the amount claimant receives from the said Insurance Company and the salvage therefrom, if any.

Dated at Seattle, Washington, this 19th day of January, 1931.

NORTHERN PACIFIC RAILWAY
COMPANY

By L. B. da PONTE
THOS. H. MAGUIRE

Its Attorneys.

State of Washington
County of King—ss.

L. B. da PONTE, being first duly sworn, on oath deposes and says:— That he is one of the attorneys for the claimant in the above entitled action; that the same is a foreign corporation, and he makes this verification for and in its behalf, being authorized so to do; that he has read the above and foregoing claim of the Northern Pacific Railway Com-

pany, knows the contents thereof, and believes the same to be true.

L. B. da PONTE

Subscribed and sworn to before me this 19th day of January, 1931.

BRUCE JENNINGS

Notary Public in and for the State of Washington, residing at Seattle, Wash. [32]

LIST OF 20 FLAT CARS DESTROYED OR DAMAGED BY FIRE, WHILE ON THE MONTBORNE LUMBER COMPANY'S TRACKS OR POSSESSION, SEPTEMBER 5, 1930.

Car No	Date Built	Original Cost	Depreciated Value	Estimated sale value before damage	Extent damaged
120411	1906	589.36	225.73	500.00	Sills burned, cannot move.
121447	1927	1220.99	1035.17	1100.00	" " " "
121818	1927	1207.15	1069.90	1100.00	" " " "
119222	1906	603.61	237.79	500.00	" " " "
120880	1902	572.77	225.73	500.00	" " " "
121116	1926	1249.16	1023.61	1100.00	" " " "
120771	1901	549.11	225.64	500.00	" " " "
120187	1906	596.27	231.85	500.00	" " " "
122011	1927	1207.15	1068.90	1100.00	" " " "
121385	1926	1241.17	1021.85	1100.00	" " " "
121379	1926	1241.17	1021.85	1100.00	" " " "
120565	1900	807.15	405.19	500.00	" " " "
121683	1927	1220.99	1035.16	1100.00	Sills damaged, can be moved.
121041	1926	1241.15	1015.60	1100.00	" " " "
122087	1927	1207.15	1068.89	1100.00	" " " "
121731	1927	1207.15	1068.90	1100.00	" " " "
121134	1926	1249.16	1023.60	1100.00	" " " "
121275	1927	1241.17	1021.86	1100.00	Broken brk cyl. " " "
121475	1927	1220.99	1035.17	1100.00	O. K.
121742	1927	1207.15	1068.90	1100.00	Totally destroyed

20879.97 16131.29 18400.00

St. Paul, Minn.

Sept. 30, 1930 [33]

EXHIBIT 3.

In the Superior Court of the State of Washington,
in and for Skagit County

No. 13524

ROY VAN MAREN,

Plaintiff,

vs.

MONTBORNE LUMBER COMPANY, a corpora-
tion,

Defendant.

AMENDED CLAIM OF NORTHERN PACIFIC
RAILWAY COMPANY.

The Northern Pacific Railway Company states that it has received payment of the sum of \$8,000.00 from North River Insurance Company on account of the twenty cars belonging to said railway company delivered by it to the Montborne Lumber Company under the interchange contract dated the 19th day of December, 1927, referred to in its original claim. It states that it has no claim and makes no claim against the Montborne Lumber Company, or the Receiver of said company, for and on account of said twenty cars, or any of them.

The Northern Pacific Railway Company further states that it neither has nor makes any claim against said Montborne Lumber Company or said receiver for or on account of any legal liability, or otherwise, for damage to or failure to return cars 120107, 121134, 122087, 121041, 121683, 120411,

121116, 120880, 121447, 121818, 120565 and 121275, and releases and discharges said Montborne Lumber Company and its receiver from any and all legal liability for or on account of damage to said cars or failure to return the same pursuant to the interchange contract above referred to or otherwise.

The Northern Pacific Railway Company further states that it has no claim and makes no claim against said Mont- [34] borne Lumber Company for and on account of any damage to or failure to return cars 120753, 121526, 121012, 121969 and 120539, and releases and discharges said Montborne Lumber Company and its receiver from any and all liability for and on account of damage to said cars or any of them, or failure to return the same, or any of them, as provided by said interchange contract, or otherwise.

The Northern Pacific Railway Company further states that it has no claim and makes no claim against said Montborne Lumber Company for and on account of any damage to or failure to return cars 121379, 121385, 122011, 121742 and 119222, and releases and discharges said Montborne Lumber Company and its receiver from any and all liability for and on account of damage to said cars or any of them, or failure to return the same, or any of them, as provided by said interchange contract, or otherwise.

The claim of the Northern Pacific Railway Company is hereby limited to the items shown in its original claim, to-wit:—for freight and demurrage \$1935.26; for bills rendered as per statement in the

sum of \$4072.70 less bill No. 89754 in the sum of \$482.13, which item is excluded from the above, and the item of indebtedness incurred subsequent to appointment of the receiver in the sum of \$169.44.

The total claim of the Northern Pacific Railway Company, which is justly due and unpaid, is the sum of \$5695.27, to which sum its said original claim is hereby amended.

Dated at Seattle, Washington, this 17th day of November, 1931.

NORTHERN PACIFIC
RAILWAY COMPANY
By L. B. DaPONTE and
THOS. H. MAGUIRE
Its Attorneys [35]

State of Washington
County of King—ss.

L. B. daPonte, being first duly sworn, on oath deposes and says:—That he is one of the attorneys for claimant in the above entitled action; that the same is a foreign corporation, and he makes this verification for and in its behalf, being authorized so to do; that he has read the above and foregoing amended claim of Northern Pacific Railway Company, knows the contents thereof, and believes the same to be true.

L. B. daPONTE

Subscribed and sworn to before me this 17th day of November, 1931.

BRUCE JENNINGS

Notary Public in and for the State of Washington, residing at Seattle.

Received a copy of the foregoing amended claim this 28th day of November, 1931.

(Sgd.) C. J. HENDERSON,

By A. McBEE

Attorneys for

The written stipulation filed on the 3rd day of October, 1934, was and is in words and figures as follows:

“In the District Court of the United States for the Western District of Washington, Northern Division.

No. 20512

GUY H. CLARK, as Receiver of the Montborne Lumber Company, a corporation,

Plaintiff,

vs.

NORTH RIVER INSURANCE COMPANY, a corporation,

Defendant.

SUPPLEMENTAL STIPULATION.

IT IS HEREBY STIPULATED by and between the parties [36] hereto by their respective counsel as follows:—

(1) That attached hereto is a copy of the policy of insurance mentioned in Paragraph (2) of the original stipulation of facts herein, and this said copy of said policy of insurance may be used on the trial of this cause for all intents and purposes the same as if the original were produced and admitted in evidence.

(2) The original stipulation of facts herein dated May 1, 1934, together with this supplemental stipulation, shall constitute the entire stipulation of facts to be submitted to the above entitled court for determination of the above entitled cause.

Dated this 3d day of October, 1934.

C. J. HENDERSON

and ALFRED McBEE

Attorneys for Plaintiff

SAWYER & CLUFF,

L. B. DaPONTE and

ROBERT S. MACFARLANE

Attorneys for Defendant [37]

No. 11187

THE NORTH RIVER INSURANCE COMPANY

Of the City of New York.

Marine Department

Appleton & Cox, Inc. Attorney

No. 1 South William Street

New York.

Incorporated 1822

Capital \$2,000,000

IN CONSIDERATION OF THE STIPULATIONS HEREIN NAMED AND OF SIX HUNDRED THIRTY Dollars Premium

DOES INSURE MONTBORNE LUMBER COMPANY

From the 8th day of August, 1930, at noon,

To the 8th day of August, 1931, at noon,

Standard Time at place of insurance against direct loss or damage as hereinafter provided, to an amount not exceeding TWENTY FIVE THOU-

SAND TWO HUNDRED Dollars, to Rolling Stock, as per schedule, including all appliances, apparatus, appurtenances, tools, spare and duplicate parts and equipment of every kind and description while on or attached to said Rolling Stock, while located as described herein, and not elsewhere.

1. Territorial Limits.

This insurance covers only while the said Rolling Stock is in, or *or* about the Round House, Shops and Turntable of the Assured or connecting lines and/or upon the line of any road owned or leased by the Assured, and its branches, spurs, side tracks and yards and upon such extensions or branches as may be constructed and/or leased by the Assured during the term of this policy and on the line of any connecting road or roads, all situated in the State of WASHINGTON but it is warranted by the Assured to notify this Company, or the agent who shall have issued the policy, in writing of their intention to use such extensions or branches as may be constructed and/or leased by the Assured prior to operation.

2. Perils Insured Against

This Policy insures only:—

Against loss or damage caused by fire, derailment or collision (coming together of cars and/or locomotives in shifting or coupling, not to be considered a collision), collapse of bridges, lightning, cyclone, tornado and flood.

It is understood and agreed that in the event of loss or damage to any part or parts of the within insured property resulting from any one accident from perils insured against, this Company shall only be liable for loss or damage in excess of Two Hundred Fifty Dollars (\$250.00). [38]

3. Conditions

(a) Notwithstanding anything in this policy to the contrary, it is warranted by the assured free from claim for loss or damage, which may be attributed to, or arise from, the act of any person acting or claiming to act, under authority from any country or people, in a state of war (whether before or after declaration of war), revolution, or internal commotion, and also from all consequences of hostilities, civil commotions, riots, and/or war-like operations, even if by lawless or unauthorized persons.

(b) It is expressly stipulated and made a condition of this contract that, in event of loss, this Company shall be liable for no greater proportion thereof than the amount insured hereunder bears to NINETY per cent (90%) of the actual value of the property described herein at the time when such loss shall happen, nor for more than the proportion which this policy bears to the total insurance thereon.

(c) It is mutually understood and agreed that this Company shall not be liable beyond the actual case value of the interest of the Assured in the property at the time of loss or damage nor exceeding what it then cost the Assured to repair or replace the same with material of like kind and quality.

(d) In the event of any but a total loss under

this policy, the amount of said loss for which this policy is liable shall be reinstated subject to all the conditions of the policy, the Assured warranting to pay pro rata premium upon the amount so reinstated from date of said loss.

(e) This entire policy shall be void if the Assured has concealed or misrepresented any material fact or circumstance concerning this insurance or the subject thereof; or in case of any fraud or false swearing by the Assured touching any matter relating to this insurance or the subject thereof, whether before or after a loss.

(f) It is warranted by the Assured that in case of loss or damage happening to the property insured hereunder, the same shall be reported as soon as the loss is known or expected to the Head Office of this Company at San Francisco, or to the Agent who shall have issued this policy. All adjusted claims shall be due and payable thirty days after presentation and acceptance of proofs of interest and loss at the office of this Company. No loss shall be paid hereunder if the Assured has collected the same from others.

(g) In the event of loss or damage caused by the risks and perils insured against, it shall be necessary for the Assured to use all lawful and proper efforts for the safeguard and recovery of the property or its value without prejudice to this insurance, and this Company will contribute to the just and reasonable charges thereof in such proportion as the sum named in this policy bears to the whole value at risk. And it is mutually agreed that the

acts of either party or their agents in securing, preserving or recovering the property insured shall not be considered or held to be either a waiver or acceptance of an abandonment. [39]

(h) No suit or action on this policy for the recovering of any claim shall be sustainable in any Court of Law or Equity unless the Assured shall have fully complied with all the foregoing requirements, nor unless commenced within twelve months next after the happening of the loss, provided that where such limitation of time is prohibited by the laws of the State wherein this policy is issued, then and in that event no suit or action under this policy shall be sustainable unless commenced within the shortest limitation permitted under the laws of such State.

(i) No person shall be deemed an Agent of this Company unless specifically authorized in writing by this Company.

(j) It is also agreed that no assignment or transfer hereof shall in any case relieve the Assured of the property hereby insured from any or all the conditions expressed in this policy, and that this policy shall be void in case of its being assigned or transferred without the written consent of this Company.

(k) This policy shall be cancelled at any time at the request of the Assured, or by this Company, by giving five (5) days' written notice of such cancellation. If this policy shall be cancelled as hereinbefore provided, the premiums having been actually paid, the unearned portion shall be returned on sur-

render of the policy, this Company retaining the customary short rate, it being mutually understood and agreed however, that a minimum earned premium of \$472.50 dollars, is guaranteed this Company, except that when this policy is cancelled by the Company by giving notice, it shall retain only the pro rata premium.

(1) This insurance to be null and void to the extent of any other insurance specific or otherwise on the within described property which would attach and cover were it not for the fact of this insurance.

Provisions Required by Law To Be Stated in This Policy:—This policy is in a stock corporation, and is issued under and in pursuance of Section 130, 131 and 132 of the Insurance Law of the State of New York.

IN WITNESS WHEREOF, the undersigned, on behalf of the said Company, have subscribed their names, in the City of NEW YORK.

This policy is void unless countersigned by the authorized agent of this company at San Francisco, California.

APPLETON & COX, INC.

Attorney

DOUGLAS F. COX

President

(Marine Dept.)

AMERICAN INSURANCE
AGENCY

By F. A. FREDERICK

Agents.

Countersigned,

PACIFIC MARINE INSURANCE
AGENCY, INC.

By S. S. HANSON

President

Date August 11th, 1930. [40]

ENDORSEMENT

It is hereby understood and agreed that clause No. 2 of the policy to which this endorsement is attached is corrected to read as follows:—

This Policy insures only against direct loss or damage by fire, derailment or collision, collapse of bridges, lightning, cyclone, tornado and flood.

It is hereby agreed that the term "Collision" as used herein, is defined as including only contact with objects, moving or stationary on rails, ties or roadbed, coming together of cars and/or locomotives in shifting or coupling being always excepted, and excluding contact with any falling objects or any objects off the rails, ties or roadbed.

It is understood and agreed that in the event of loss or damage to any part or parts of the within insured property resulting from any one accident from perils insured against, \$250.00 shall be deducted from any claim on locomotives, \$250.00 from any other piece of equipment valued at \$7,500.00 or over, \$50.00 from any other piece of equipment valued at less than \$7,500.00, but not more than \$250.00 in any one accident.

All other terms and conditions remaining unchanged.

This slip is attached to and made a part of Policy No. 11187, issued to MONTBORNE LUMBER COMPANY by the NORTH RIVER INSURANCE COMPANY.

Dated at SEATTLE, WASH, AUGUST 11th, 1930.

(Marine Dept.)

AMERICAN INSURANCE
AGENCY

By F. A. FREDERICK

Agents

ENDORSEMENT

It is also understood and agreed that this policy covers the legal liability only of the assured on logging cars owned by others in the possession of the assured, but it is a warranty of this insurance that the insured shall not have at risk an average of more than twelve (12) cars at any one time.

All others terms and conditions remaining unchanged.

This slip is attached to and forms part of Policy No. 11187 of the NORTH RIVER INSURANCE COMPANY issued to MONTBORNE LUMBER COMPANY.

Seattle, Wash. AUGUST 11th, 1930.

(Marine Dept.)

AMERICAN INSURANCE
AGENCY

By F. A. FREDERICK

Agent [41]

(Written on reverse side of policy)

Each Unit Separately Insured

Amount

of

Trade Name	Year Built	Shop Number	Ton- nage	Insur- ance	Rate	Pre- mium
1 Shay loco-						
motive		#2703	90 Ton	\$15,000	2½%	\$375.00
12 CARS OWNED						
by any						
others than the Assured,						
consisting principally of						
Northern Pacific flat cars,						
main line tanks, and coal						
gondolas, being an equal						
amount of coverage on						
each				\$10,200	2½%	\$255.00
Total				\$25,200.		\$630.00

[42]

No other evidence was offered by either party and thereupon both plaintiff and defendant, through their respective attorneys, made motions for a declaration of law and for special findings in accordance with said stipulations, and each of them, and for judgment in favor of their respective clients, and said motions were argued orally to the Court.

That thereupon, pursuant to motions made by the respective parties through their respective attorneys, the Court ordered that the cause be submitted upon briefs with periods then and there fixed by the Court, and that pursuant to such order briefs on behalf of the respective parties were filed within the time limited by said order, in which briefs motions

for judgment in favor of the respective parties were incorporated by their respective attorneys, and upon the filing of the last brief the cause was submitted.

Thereafter, and on the 20th day of October, 1934, the said Honorable John C. Bowen made and filed his Memorandum Decision of the above-entitled cause, in words and figures as follows:

“In the District Court of the United States, for the Northern District of Washington, Northern Division.

No. 20512

GUY H. CLARK, as Receiver of the Montborne Lumber Company, a corporation,

Plaintiff,

vs.

NORTH RIVER INSURANCE COMPANY, a corporation,

Defendant.

MEMORANDUM DECISION

Filed: October 20, 1934.

C. J. Henderson, Mount Vernon, Washington.

Alfred McBee, Mount Vernon, Washington.

Attorneys for Plaintiff.

L. B. daPonte, Seattle, Washington,

Robert S. Macfarlane, Seattle, Washington.

Sawyer & Cluff, San Francisco, California.

Attorneys for Defendant. [43]

The Montborne Lumber Company, of which the plaintiff is receiver, procured a policy of insur-

ance from the defendant insuring the Lumber Company against loss or damage caused by fire, derailment or collision, collapse of bridges, lightning, cyclone, tornado and flood, covering a Shay locomotive engine owned by the Lumber Company valued at \$7,000.00, and twelve logging flat cars loaned by Northern Pacific Railway Company to the Lumber Company under a sort of license or bailment agreement requiring the Lumber Company to pay the Railway Company for all damages which the cars might sustain from any cause while in the possession of the Lumber Company. The policy had attached to it the following endorsement in writing: "It is also understood and agreed that this policy covers the legal liability only of the assured on logging cars owned by others * * *".

While the policy was in force a forest fire destroyed bridges on the Lumber Company's railroad, marooning the locomotive up in the woods, and it would have cost more to repair the bridges for the purpose of bringing the locomotive out of the woods than the locomotive is worth, it being agreed that its value is \$7000.00. The total loss and damage caused by derailment and/or the fire to the logging flat cars belonging to the Railway Company was the total sum of \$8000.00. The locomotive itself was never in contact with the fire and sustained no physical damage as a result of the fire, but the destruction of the railroad bridges was caused by the fire.

The plaintiff, as receiver of the Lumber Company, sued the defendant under the policy for \$7000.00, the total value of the locomotive owned by it, and for [44] \$8000.00, the total loss and damage to the

logging flat cars owned by the Railway Company, alleging as to the flat cars "That as a result of said damage to said cars, the said assured has been and is now unable to return the same to the Northern Pacific Railway Company in as good condition as they were at the time of delivery to assured, or at all, and that by reason of said facts assured is legally liable to said Northern Pacific Railway Company in excess of * * *". The case was tried before the court without a jury, on stipulated facts. The defendant has never paid anything on account of the locomotive, but the defendant settled with the Railway Company direct for the damage to the logging flat cars and the Railway Company filed in the receivership proceedings a release and discharge of the Lumber Company and its receiver, the plaintiff, in respect to any and all legal liability for and on account of the said cars.

As to the locomotive, the liability of the defendant Insurance Company in this case depends upon whether or not the loss or damage sued for (the total value of the locomotive) was proximately caused by the fire, which did no physical damage to the locomotive itself but which did destroy the bridges and thereby made it impossible to bring the locomotive out of the woods without rebuilding the bridges at a cost in excess of the value of the locomotive. The court is advised of no authority directly controlling, but the general rule, as stated in *Ruling Case Law*, is that "* * *" to render a fire the immediate or proximate cause of loss or damage, it is not necessary that any part of the insured property should be actually ignited or con-

sumed by fire. Insurance against loss by fire includes loss where the [45] cause insured against was the means or agency in causing the loss, even though it was entirely due to some other active, efficient cause which made use of it or set it in motion." 14 R. C. L. 1216. To the same effect is *Ermentraut v. Girard Fire Ins. Co.* 65 N.W. 635 (Minn. 1895); see also *Hall v. Great American Ins. Co.* 252 N.W. 763 (Iowa 1934). It is also a fundamental principle of insurance law that "* * * a loss by fire includes every loss necessarily following from the occurrence of a fire if it arises directly and immediately from the peril or necessarily from incidental and surrounding circumstances, the operation and influence of which could not be avoided * * *", such as any and every expense borne by and chargeable upon the owner of a thing insured, as a direct and immediate consequence of the peril insured against. 6 Couch on Insurance, Sec. 1467, page 5304; *Hale v. Washington Ins. Co.*, 11 Fed. Cases page 189, Case No. 5916.

In the absence of specific authority to the contrary, it seems to the court that the value of the locomotive itself has been as effectually destroyed by the destruction of the bridges and consequent marooning of the locomotive as if the fire had reduced to a molten mass, the component materials of the locomotive, that such destruction of the locomotive was caused directly and proximately by the fire, and that, contrary to defendant's contention, not merely the profitable use of the locomotive has been interrupted. The court so finds and concludes that

the defendant is liable to the plaintiff in the sum of \$7000.00 for the value of the locomotive.

As to the logging flat cars owned by the Railway Company, it seems to me that in the final analysis the [46] question of defendant's liability under the policy must turn upon the effect to be given to the endorsement on the policy that "It is also understood and agreed that this policy covers the legal liability only of the assured on logging cars owned by others * * *". In the law relating to insurance as well as other contracts, the rule is that specific provisions must control over general provisions, and construing the policy, together with said endorsement, it is obvious that the parties intended that liability of the assured rather than loss or damage to the insured, was the thing insured against. By reason of the settlement of the question of damage to the cars made direct by the defendant with the Railway Company, and the release and discharge of the Lumber Company and the plaintiff receiver by the Railway Company, controlling evidence of which may be found by a reference to "Exhibit 3" attached to the stipulation of facts filed herein May 1, 1934, plaintiff has wholly failed to prove, what was required of him, that, as a result of the damage to the cars, assured is legally liable to the Railway Company in any sum. Plaintiff, therefore, has not sustained the burden of proof as to his claim or claims set forth in the complaint herein as to the cars, no matter on what theory, nor under what kind or nature of an insurance policy, such claim or claims may have been asserted. In fact, all of the proof on this question conclusively shows that the Lumber Company and plain-

tiff have no legal liability whatsoever to the Railway Company or the owner of the cars. It, therefore, is unimportant whether the policy was an indemnity, a liability, or a so-called "fire policy", because, as to the cars, plaintiff has proved no facts warranting recovery under any theory or under any kind of [47] policy. On this issue as to the cars, the judgment of the court will be for the defendant.

Counsel may propose appropriate findings, conclusions and judgment.

JOHN C. BOWEN

United States District Judge."

Thereafter, on the 31st day of October, 1934, the said Honorable John C. Bowen made and entered an order extending time within which to serve, settle, file or sign Findings, Judgment and Bill of Exceptions, and extending the then term of court for said purpose, in words and figures as follows:

"In the District Court of the United States for the Western District of Washington, Northern Division.

No. 20512

GUY H. CLARK, as Receiver of the Montborne Lumber Company a corporation,

Plaintiff,

vs.

NORTH RIVER INSURANCE COMPANY, a corporation,

Defendant.

ORDER

This matter coming on to be heard on motion of plaintiff and defendant for extension of time to

serve, settle, file or sign findings, judgment and bill of exceptions, and for extension of term, and the court being fully advised in the premises,

NOW, THEREFORE, it is

ORDERED that the time of the plaintiff and defendant to serve, settle, file or sign findings, judgment and bill of exceptions herein be and the same is hereby extended [48] for ninety (90) days from October 31, 1934; and it is

Further ORDERED that the present term of this court be and the same hereby is extended for said purposes until the expiration of said ninety days.

DONE IN OPEN COURT this 31st day of October, 1934.

JOHN C. BOWEN

District Judge

Presented by:—

ROBERT S. MACFARLANE

At request of Alfred McBee,
Attorney for Plaintiff.”

That thereafter on the 16th day of November, 1934, defendant, through its attorneys, served plaintiff with a copy of its proposed Findings of Fact and Conclusions of Law, which said proposed Findings of Fact and Conclusions of Law were signed by the court on January 14, 1935, pursuant to waiver of notice of presentation, in words and figures as follows:—

“In the District Court of the United States for the Western District of Washington, Northern Division.

No. 20512

GUY H. CLARK, as Receiver of the Montborne Lumber Company, a corporation,

Plaintiff,

v.

NORTH RIVER INSURANCE COMPANY, a corporation,

Defendant.

FINDINGS OF FACT and CONCLUSIONS OF
LAW

The above entitled matter regularly coming on to be heard for the entry of Findings of Fact and Conclusions of Law, plaintiff appearing by his counsel, C. J. Henderson and Alfred McBee, and defendant appearing by its counsel, Sawyer & Cluff, L. B. daPonte and Robert S. Macfarlane, [49] and it appearing that the above entitled cause came on to be heard before the undersigned judge of the above entitled court on the 3rd day of October, 1934, and it further appearing that all of the facts were incorporated in written stipulations filed in the above entitled cause on the 1st day of May, 1934, and the 3rd day of October, 1934, and the parties having fully presented and argued the cause, and the court heretofore, to-wit, on October 20, 1934, having entered and filed its memorandum decision

herein, and the court being fully advised in the premises, now makes and enters the following

FINDINGS OF FACT.

I.

That on or about August 11, 1930, a policy of insurance was effected by the Montborne Lumber Company, (hereinafter called Lumber Company), with the defendant, which policy of insurance is in words and figures as follows:—

No. 11187

THE NORTH RIVER INSURANCE COMPANY
Of the City of New York.

—
Marine Department
Appleton & Cox, Inc. Attorney
No. 1 South William Street
New York.

Incorporated 1822

Capital \$2,000,000

IN CONSIDERATION OF THE STIPULATIONS HEREIN NAMED AND OF SIX HUNDRED THIRTY Dollars Premium

DOES INSURE MONTBORNE LUMBER COMPANY

From the 8th day of August, 1930, at noon,
To the 8th day of August, 1931, at noon,
Standard Time at place of insurance against direct loss or damage as hereinafter provided, to an

amount not exceeding TWENTY FIVE THOUSAND TWO HUNDRED DOLLARS, to Rolling Stock, as per schedule, including all appliances, apparatus, appurtenances, tools, spare and duplicate [50] parts and equipment of every kind and description while on or attached to said Rolling Stock, while located as described herein, and *no* elsewhere.

1. Territorial Limits.

This insurance covers only while the said Rolling Stock is in, on or about the Round House, Shops and Turntable of the Assured or connecting lines and/or upon the line of any road owned or leased by the Assured, and its branches, spurs, side tracks and yards and upon such extensions or branches as may be constructed and/or leased by the Assured during the term of this policy and on the line of any connecting road or roads, all situated in the State of WASHINGTON but it is warranted by the Assured to notify this Company, or the agent who shall have issued the policy, in writing of their intention to use such extensions or branches as may be constructed and/or leased by the Assured prior to operation.

2. Perils Insured Against

This Policy Insures only:—

Against loss or damage caused by fire, derailment or collision (coming together of cars and/or locomotive in shifting or coupling, not to be considered a collision), collapse of bridges, lightning, cyclone, tornado and flood.

It is understood and agreed that in the event of loss or damage to any part or parts of the within insured property resulting from any one accident from perils insured against, this Company shall only be liable for loss or damage in excess of Two Hundred Fifty Dollars (\$250.00).

3. Conditions

(a) Notwithstanding anything in this policy to the contrary, it is warranted by the assured free from claim for loss or damage, which may be attributed to, or arise from, the act of any person acting or claiming to act, under authority from any country or people, in a state of war (whether before or after declaration of war), revolution, or internal commotion, and also from all consequences of hostilities, civil commotions, riots, and/or war-like operations, even if by lawless or unauthorized persons.

(b) It is expressly stipulated and made a condition of this contract that, in event of loss, this Company shall be liable for no greater proportion thereof than the amount insured hereunder bears to NINETY per cent (90%) of the actual value of the property described herein at the time when such loss shall happen, nor for more than the proportion which this policy bears to the total insurance thereon.

(c) It is mutually understood and agreed that this Company shall not be liable beyond the actual

cash value of the interest of the Assured in the property at the time of loss or damage nor exceeding what it then cost the Assured to repair or replace the same with material of like kind and quality.

(d) In the event of any but a total loss under this policy, the amount of said loss for which this policy is liable shall be reinstated subject to all the conditions of the policy, the Assured warranting to pay pro rata premium upon the amount so reinstated from date of said loss. [51]

(e) This entire policy shall be void if the Assured has concealed or misrepresented any material fact or circumstance concerning this insurance or the subject thereof; or in case of any fraud or false swearing by the Assured touching any matter relating to this insurance or the subject thereof, whether before or after a loss.

(f) It is warranted by the Assured that in case of loss or damage happening to the property insured hereunder, the same shall be reported as soon as the loss is known or expected to the Head Office of this Company at San Francisco, or to the Agent who shall have issued this policy. All adjusted claims shall be due and payable thirty days after presentation and acceptance of proofs of interest and loss at the office of this Company. No loss shall be paid hereunder if the Assured has collected the same from others.

(g) In the event of loss or damage caused by the risks and perils insured against, it shall be necessary for the Assured to use all lawful and proper efforts for the safeguard and recovery of the property or its value without prejudice to this insurance, and this Company will contribute to the just and reasonable charges thereof in such proportion as the sum named in this policy bears to the whole value at risk. And it is mutually agreed that the acts of either party or their agents in securing, preserving or recovering the property insured shall not be considered or held to be either a waiver or acceptance of an abandonment.

(h) No suit or action on this policy for the recovery of any claim shall be sustainable in any Court of Law or Equity unless the Assured shall have fully complied with all the foregoing requirements, nor unless commenced within twelve months next after the happening of the loss, provided that where such limitation of time is prohibited by the laws of the State wherein this policy is issued, then and in that event no suit or action under this policy shall be sustainable unless commenced within the shortest limitation permitted under the laws of such State.

(i) No person shall be deemed an Agent of this Company unless specifically authorized in writing by this Company.

(j) It is also agreed that no assignment or transfer hereof shall in any case relieve the Assured of the property hereby insured from any or all the

conditions expressed in this policy, and that this policy shall be void in case of its being assigned or transferred without the written consent of this Company.

(k) This policy shall be cancelled at any time at the request of the Assured, or by this Company, by giving five (5) days' written notice of such cancellation. If this policy shall be cancelled as hereinbefore provided, the premiums having been actually paid, the unearned portion shall be returned on surrender of the policy, this Company retaining the customary short rate, it being mutually understood and agreed however, that a minimum earned premium of \$472.50 dollars is guaranteed this Company, except that when this policy is cancelled by the Company by giving notice, it shall retain only the pro [52] rata premium.

(l) This insurance to be null and void to the extent of any other insurance specific or otherwise on the within described property which would attach and cover were it not for the fact of this insurance.

Provisions Required by Law to Be Stated in This Policy:—This policy is in a stock corporation, and is issued under and in pursuance of Section 130, 131 and 132 of the Insurance Law of the State of New York.

IN WITNESS WHEREOF, the undersigned, on behalf of the said Company, have subscribed their names, in the City of NEW YORK.

This policy is void unless countersigned by the authorized agent of this company at San Francisco, California.

APPLETON & COX, INC.

Attorney

DOUGLAS F. COX

President

(Marine Dept.)

AMERICAN INSURANCE

AGENCY

By F. A. FREDERICK

Agents.

Countersigned,

PACIFIC MARINE

INSURANCE AGENCY, INC.

By S. S. HANSEN

President

Date August 11th, 1930.

ENDORSEMENT

It is hereby understood and agreed that clause No. 2 of the policy to which this endorsement is attached is corrected to read as follows:

This Policy insures only against direct loss or damage by fire, derailment or collision, collapse of bridges, lightning, cyclone, tornado and flood.

It is hereby agreed that the term "Collision" as used herein, is defined as including only contact with objects, moving or stationary on rails, ties or roadbed, coming together of cars and/or locomotives in shifting or coupling being always excepted,

and excluding contact with any falling objects or any objects off the rails, ties or roadbed.

It is understood and agreed that in the event of loss or damage to any part or parts of the within insured property resulting from any one accident from perils insured against, \$250.00 shall be deducted from any claim on locomotives, \$250.00 from any other piece of equipment valued at \$7,500.00 or over, \$50.00 from any other piece of equipment valued at less than \$7,500.00, but not more than \$250.00, in any one accident.

All other terms and conditions remaining unchanged.

This slip is attached to and made a part of Policy No. 11187, issued to MONTBORNE LUMBER COMPANY by the NORTH RIVER INSURANCE COMPANY. [53]

Dated at SEATTLE, WASH. AUGUST 11th, 1930.

(Marine Dept.)

AMERICAN INSURANCE
AGENCY

By F. A. FREDERICK

Agents

ENDORSEMENT

It is also understood and agreed that this policy covers the legal liability only of the assured on logging cars owned by others in the possession of the assured, but it is a warranty of this insurance that the insured shall not have at risk an average of more than twelve (12) cars at any one time.

All other terms and conditions remaining unchanged.

This slip is attached to and forms part of Policy No. 11187 of the NORTH RIVER INSURANCE COMPANY issued to MONTBORNE LUMBER COMPANY.

Seattle, Wash. AUGUST 11th, 1930.

(Marine Dept.)

AMERICAN INSURANCE
AGENCY

By F. A. FREDERICK

Agent

(Written on reverse side of Policy)

Each Unit Separately Insured

Amount
of

Trade Name	Year Built	Shop Number	Ton- nage	Insur- ance	Rate	Pre- mium
1 Shay loco- motive		#2703	90 Ton	\$15,000.00	2½%	\$375
12 CARS OWNED by any others than the Assured, consisting principally of Northern Pacific flat cars, main line tanks, and coal gondolas, being an equal amount of coverage on each				\$10,200.00	2½%	\$255
Total				\$25,200.00		\$630.

II.

That the Lumber Company at all times herein in question was engaged in the business of logging near Montborne, Skagit County, Washington, and in connection with said operations said Lumber Company built a logging railroad back into the timber to the scene of its logging operations from the station of Montborne on the Seattle-Sumas main line of the Northern [54] Pacific Railway Company.

III.

That on or about September 4, 1930, a forest fire broke out in the holdings of the Lumber Company and spread onto and over portions of the logging railroad owned and operated by the Lumber Company, destroying certain bridges and trestles of said logging railroad.

IV.

That the Lumber Company owned a certain 90-ton Shay locomotive, shop No. 2703, which locomotive at the time of the fire heretofore mentioned was situated on the logging railroad in the woods; and that by reason of the aforementioned destruction of certain bridges and trestles on the logging railroad between the locomotive and Montborne station, the said locomotive was marooned. The locomotive itself was never in contact with the fire and sustained no physical damage as a result of the fire. The cost of sufficiently repairing the said bridges

and trestles in order to get the locomotive out of the woods and down to Montborne station would exceed the value of the locomotive. That at the time of the fire in question the reasonable market value of the said locomotive was \$7,000.00.

V.

That the Northern Pacific Railway Company, (hereinafter called the Railway Company), is a corporation engaged in business as a common carrier railroad, and carries on its business in Skagit County and in the State of Washington and elsewhere. That the said Railway Company and the Lumber Company entered into a certain interchange agreement dated December 19, 1927, in words and figures as follows:— [55]

CONTRACT made this 19th day of December, A.D. 1927, between the NORTHERN PACIFIC RAILWAY COMPANY, a Wisconsin corporation, hereinafter called "Railroad" and the MONTBORNE LUMBER COMPANY, a Washington corporation, hereinafter called "Lumber Company."

In consideration of the mutual dependent promises stated in this contract the parties agree:—

I.

Connections between the tracks of the parties hereto have been installed at Montborne, Washington, under the provisions of a contract between them dated November 22, 1926, and the parties agree to interchange carload business at such point through such connections.

II.

The Lumber Company agrees to pay the Railroad for all damage which cars delivered to it by the Railroad through such connections may sustain from any cause whatever while in its possession and to indemnify and protect the Railroad against any claim for personal injury or death on account of alleged defects in such equipment and to return promptly all cars received from the Railroad and be governed by tariff provisions relating to demurrage.

GTR FRB WEC JEC AVB FEW

III.

For the purpose of fixing liability for loss and damage to cars and their loads, cars and loads placed by the Railroad at the point of interchange for movement over the logging railroad of the Lumber Company or for the use of the Lumber Company shall be deemed to be in the Lumber Company's possession and to continue in its possession until the railroad shall move said cars from said point of interchange on to its own main track.

IN WITNESS WHEREOF the parties hereto have caused this contract to be executed by officers thereunto duly authorized on the day and year first above written.

NORTHERN PACIFIC
RAILWAY COMPANY

By F. F. WILLIAMSON

Its Vice President

WITNESSES:—

T. K. YOUNG

R. D. VAN VOORHIS

MONTBORNE LUMBER
COMPANY

By THOMAS SMITH

Its President

WITNESSES;—

FRANK F. DAY

L. G. HARVEY

That said interchange agreement fully sets forth the rights and liabilities of the Lumber Company and the Railway Company with respect to cars and equipment belonging to the Railway Company used by the Lumber Company, which said agreement was in full force and effect at all times material to [56] this litigation.

VI.

That on August 11, 1930, and for a long time prior thereto, and until the time of the fire before mentioned, the Railway Company furnished the Lumber Company its flat cars, main line tanks and coal gondolas for the purpose of loading and/or unloading freight under said interchange agreement; that the Lumber Company did not own any logging flat cars, main line tanks or coal gondolas, and that all rolling equipment of said character used or intended to be used at any time material to this litigation upon the logging railroad of the Lumber Company was rolling equipment owned

by the Railway Company and furnished pursuant to the said interchange agreement.

VII.

That it was the practice and procedure of both parties under the interchange agreement for the Railway Company to deliver empty logging flat cars to the Lumber Company upon the siding at Montborne station; that thereafter the Lumber Company, with its own locomotive, took said logging flat cars from said siding over its logging railroad into the timber to the scene of its operations for the purpose of loading; that after loading, the logging flat cars were thereupon taken by the locomotive of the Lumber Company back to the siding at Montborne station, from which siding said cars were picked up by the Railway Company for further transportation over its railroad to destination.

VIII.

That this practice and procedure and this form of interchange agreement, with substantially identical provisions, was usual and customary between logging railroads and common carrier railroads in Western Washington at all times [57] material to this litigation.

IX.

That on or about August 30, 1930, five certain logging flat cars, (N.P. 120753, N.P. 121526, N.P. 121012, N.P. 121969, N.P. 120539), belonging to

the Railway Company and in the possession of the Lumber Company pursuant to the terms of the interchange agreement, were derailed, and that by reason of said derailment were damaged in the amount of \$482.13, which damage was fully repaired by the Railway Company at its expense.

X.

That on or about September 4, 1930, said cars which had been derailed and repaired, together with other logging flat cars, (N.P. 120107, N.P. 121134, N.P. 122087, N.P. 121041, N.P. 121683, N.P. 120411, N.P. 121116, N.P. 120880, N.P. 121447, N.P. 121818, N.P. 120565, N.P. 121275, N.P. 121379, N.P. 121385, N. P. 122011, N.P. 121742 and N.P. 119222), totaling 22 logging flat cars, were destroyed by the forest fire heretofore mentioned, which said logging flat cars were the property of the Railway Company, and were in the possession of the Lumber Company pursuant to the terms of the interchange agreement heretofore mentioned.

XI.

That no flat cars, main line tanks or coal gondolas other than those herein described belonging to others than the Lumber Company were upon the logging railroad or in the possession of the Lumber Company at the time of the fire.

XII.

That the loss and damage caused by derailment

and/or fire to all of said cars was in the total sum of \$8,000.00 [58]

XIII.

That shortly after the said fire said Lumber Company became hopelessly insolvent and went into receivership and plaintiff is now the receiver of said Lumber Company, liquidating the same.

XIV.

That on or about January 20, 1931, there was filed in the proper proceeding involving the insolvency and receivership of the Lumber Company, a claim by the Northern Pacific Railway Company against the Lumber Company, which said claim is in words and figures as follows:—

In the Superior Court of the State of Washington
in and for Skagit County.

No. 13524

ROY VAN MAREN,

Plaintiff,

vs.

MONTBORNE LUMBER COMPANY,
a corporation,

Defendant.

CLAIM OF NORTHERN PACIFIC RAILWAY
COMPANY

Pursuant to the court's order and the notice of receivers dated the 21st day of October, 1930, that

claims duly verified with proper vouchers attached be presented on or before January 24, 1931, the Northern Pacific Railway Company states the following:—

There is attached hereto a statement in detail with vouchers attached showing an amount of \$6,177.40 due from the Montborne Lumber Company to Northern Pacific Railway Company on account of the items shown in the detailed statement and vouchers attached hereto, and said details and vouchers are self-explanatory.

In addition to said amount, the Montborne Lumber Company has in its possession 20 cars belonging to the Northern Pacific Railway Company delivered by claimant to said Montborne Lumber Company under the interchange contract dated the 19th day of December, 1927, a copy of which is in the possession of the Montborne Lumber Company. Said cars [59] have been more or less damaged as shown by the statement hereto attached. Claimant states that there is a policy of insurance on said cars, or some of them, issued to Montborne Lumber Company by the North River Insurance Company, and this company claims that said policy inures to its benefit and that it is entitled to the protection of said policy on said cars and to the money due thereon. Claimant has not received any sums on account of said insurance and cannot state when it will receive anything thereon, nor the amount thereof, and therefore cannot at this time

state what balance will be due from the Montborne Lumber Company and its receivers on account of the damage or destruction of said cars. Claimant further shows that there will be salvage from said cars, which should be deducted from said account, but cannot state at this time what the amount of said salvage will be, nor the cost of recovering said cars. Claimant will file an amended claim at a later date showing the balance due from the Montborne Lumber Company on account of said cars after deducting the amount claimant receives from the said Insurance Company and the salvage therefrom, if any.

Dated at Seattle, Washington, this 19th day of January, 1931.

NORTHERN PACIFIC
RAILWAY COMPANY

By: L. B. daPONTE

THOS. H. MAGUIRE

Its Attorneys.

State of Washington
County of King—ss.

L. B. daPonte, being first duly sworn, on oath deposes and says:—That he is one of the attorneys for the claimant in the above entitled action; that the same is a foreign corporation, and he makes this verification for and in its behalf, being authorized so to do; that he has read the above and foregoing claim of the Northern Pacific Railway Com-

pany, knows the contents thereof, and believes the same to be true.

L. B. daPONTE

Subscribed and sworn to before me this 19th day of January, 1931.

BRUCE JENNINGS

Notary Public in and for the State of Washington, residing at Seattle, Wash. [60]

LIST OF 20 FLAT CARS DESTROYED OR DAMAGED BY FIRE, WHILE ON THE MONTBORNE LUMBER COMPANY'S TRACKS OR POSSESSION, SEPTEMBER 5, 1930.

Car No	Date Built	Original cost	Depreciated Value	Estimated sale value before damage	Extent Damaged			
120411	1906	598.36	225.73	500.00	Sills	burned, cannot move.		
121447	1927	1220.99	1035.17	11.00.00	"	"	"	"
121818	1927	1207.15	1069.90	1100.00	"	"	"	"
119222	1906	603.61	237.79	500.00	"	"	"	"
120880	1902	572.77	225.73	500.00	"	"	"	"
121116	1926	1249.16	1023.61	1100.00	"	"	"	"
120771	1901	549.11	225.64	500.00	"	"	"	"
120187	1906	596.27	231.85	500.00	"	"	"	"
122011	1927	1207.15	1068.90	1100.00	"	"	"	"
121385	1926	1241.17	1021.85	1100.00	"	"	"	"
121379	1926	1241.17	1021.85	1100.00	"	"	"	"
120565	1900	807.15	405.19	500.00	"	"	"	"
121683	1927	1220.99	1035.16	1100.00	Sills	damaged, can be moved.		
121041	1926	1241.15	1015.60	1100.00	"	"	"	"
122087	1927	1207.15	1068.89	1100.00	"	"	"	"
121731	1927	1207.15	1068.90	1100.00	"	"	"	"
121134	1926	1249.16	1023.60	1100.00	"	"	"	"
121275	1927	1241.17	1021.86	1100.00	Broken brk cyl.	"	"	"
121475	1927	1220.99	1035.17	1100.00	O. K.			
121742	1927	1207.15	1068.90	1100.00	Totally destroyed.			

20879.97 16131.29 18400.00

St. Paul, Minn.

Sept. 30, 1930.

That the detailed statement and voucher referred to in Paragraph 2 of said claim refer to demurrage and other items not material to the present litigation and are therefore by agreement of counsel eliminated therefrom.

XV.

That on or about November 28, 1931, there was properly and timely filed in the proper proceeding involving the insolvency and receivership of the Lumber Company, a waiver and release of the claims of the Railway Company against the Lumber Company on account of any legal liability or otherwise for damage to any of said logging flat cars for any cause whatsoever, which waiver and release of claims [61] designated "Amended Claim of the Northern Pacific Railway Company" is in words and figures as follows:—

In the Superior Court of the State of Washington
in and for Skagit County.

No. 13524

ROY VAN MAREN,

Plaintiff,

vs.

MONTBORNE LUMBER COMPANY,
a corporation,

Defendant.

AMENDED CLAIM OF NORTHERN PACIFIC
RAILWAY COMPANY

The Northern Pacific Railway Company states that it has received payment of the sum of \$8,000.00

from North River Insurance Company on account of the twenty cars belonging to said railway company delivered by it to the Montborne Lumber Company under the interchange contract dated the 19th day of December, 1927, referred to in its original claim. It states that it has no claim and makes no claim against the Montborne Lumber Company, or the Receiver of said company for and on account of said twenty cars, or any of them.

The Northern Pacific Railway Company further states that it neither has nor makes any claim against said Montborne Lumber Company or said receiver for or on account of any legal liability, or otherwise, for damage to or failure to return cars 120107, 121134, 122087, 121041, 121683, 120411, 121116, 120880, 121447, 121818, 120565 and 121275, and releases and discharges said Montborne Lumber Company and its receiver from any and all legal liability for or on account of damage to said cars or failure to return the same pursuant to the interchange contract above referred to, or otherwise.

The Northern Pacific Railway Company further states that it has no claim and makes no claim against said Montborne Lumber Company for and on account of any damage to or failure to return cars 120753, 121526, 121012, 121969 and 120539, and releases and discharges said Montborne Lumber Company and its receiver from any and all liability for and on account of damage to said cars or any of them, or failure to return the same, or any of them, as provided by said interchange contract, or otherwise.

The Northern Pacific Railway Company further states that it has no claim and makes no claim against said Montborne Lumber Company for and on account of any damage to or failure to return cars 121379, 121385, 122011, 121742 and 119222, and releases and discharges said Montborne Lumber Company and its receiver from any and all liability for and on account of damage to said cars or any of them, or failure to return the same, or any of them, as provided by said interchange contract, or otherwise. [62]

The claim of the Northern Pacific Railway Company is hereby limited to the items shown in its original claim, to-wit:—for freight and demurrage \$1935.26; for bills rendered as per statement in the sum of \$4072.70 less bill No. 89754 in the sum of \$428.13, which item is excluded from the above, and the item of indebtedness incurred subsequent to appointment of the receiver in the sum of \$169.44.

The total claim of the Northern Pacific Railway Company, which is justly due and unpaid, is the sum of \$5695.27, to which sum its said original claim is hereby amended.

Dated at Seattle, Washington, this 17th day of November, 1931.

NORTHERN PACIFIC
RAILWAY COMPANY

By: L. B. daPONTE and
THOS. H. MAGUIRE

Its Attorneys

State of Washington

County of King—ss.

L. B. daPonte, being first duly sworn, on oath deposes and says:—That he is one of the attorneys for claimant in the above entitled action; that the same is a foreign corporation, and he makes this verification for and in its behalf, being authorized so to do; that he has read the above and foregoing amended claim of Northern Pacific Railway Company, knows the contents thereof, and believes the same to be true.

L. B. daPONTE

Subscribed and sworn to before me this 17th day of November, 1931.

BRUCE JENNINGS

Notary Public in and for the State of Washington, residing at Seattle

Received a copy of the foregoing amended claim this 28th day of November, 1931.

(Sgd.) C. J. HENDERSON

By A. McBEE

That the cars itemized and listed in said amended claim are the cars damaged by derailment and fire as heretofore described herein; that the amounts claimed as shown in the last [63] two paragraphs of said amended claim are in addition to all loss or damage on account of the said logging flat cars, that said items are immaterial to this litigation, and refer to demurrage and other like charges.

XVI.

That the defendant Insurance Company paid to the Railway Company on February 26, 1931 the sum of \$8,000.00 in full settlement and satisfaction of any and all claims said Railway Company might have against it or the Lumber Company or on account of the damage to or destruction or loss of any and all cars of said Railway Company covered by the said policy of insurance; that said settlement and satisfaction made by the defendant Insurance Company was without the consent of the receiver.

XVII.

By reason of all of the foregoing, the defendant Insurance Company has refused to pay or recognize the claim of the Lumber Company now being prosecuted seeking \$7,000.00, because of the aforesaid Shay locomotive and \$8,000.00 because of the derailment and burning of the aforesaid logging flat cars.

DONE IN OPEN COURT this 14 day of January, 1935.

JOHN C. BOWEN

District Judge

Notice of Presentation Waived

C. J. HENDERSON

ALFRED McBEE

Attys. for Pltf.

Presented:—

ROBERT S. MACFARLANE

From the foregoing Findings of Fact, the court makes and enters the following [64]

CONCLUSIONS OF LAW

I.

Plaintiff is entitled to judgment against the defendant for the sum of Seven Thousand Dollars (\$7,000.00), together with interest from date thereof, together with his costs and disbursements as provided by law.

To the foregoing Conclusion of Law the defendant excepts and its exception is by the court allowed.

DONE IN OPEN COURT this 14 day of January, 1935.

JOHN C. BOWEN

District Judge

Presented by:—

ROBERT S. MACFARLANE

Notice of Presentation Waived.

C. J. HENDERSON

ALFRED McBEE

That on aforesaid 14th day of January, 1935, when the matter of signing Findings of Fact, Conclusions of Law and Judgment came on to be heard before the court, defendant presented to the court its motion theretofore served on attorneys for plaintiff for entry of Conclusions of Law and Judgment as thereto attached, which said motion and conclusions of law and judgment attached are in words and figures as follows:—

“In the District Court of the United States for the
Western District of Washington, Northern
Division.

No. 20512

GUY H. CLARK, as Receiver of the Montborne
Lumber Company, a corporation,

Plaintiff,

vs.

NORTH RIVER INSURANCE COMPANY,
a corporation,

Defendant.

MOTION FOR THE ENTRY OF CONCLU-
SIONS OF LAW AND JUDGMENT [65]

Comes now the defendant and moves the court for
the entry of the hereto attached conclusions of law
and judgment.

Dated this 14th day of January, 1935.

L. B. daPONTE,
SAWYER & CLUFF and
ROBERT S. MACFARLANE
Attorneys for Defendant.

Service of copy of the above motion, and attached
Conclusions of Law and Judgment is hereby
acknowledged this 14th day of January, 1935, by
receipt this date of true and correct copies thereof.

C. J. HENDERSON
ALFRED McBEE

Attorneys for Plaintiff.

Motion denied, Jan. 14, 1935.

JOHN C. BOWEN,
Judge”

(Attached to Motion)

“In the District Court of the United States for
the Western District of Washington, Northern
Division.

No. 20512

GUY H. CLARK, as Receiver of the Montborne
Lumber Company, a corporation,

Plaintiff,

v.

NORTH RIVER INSURANCE COMPANY,
Defendant.

CONCLUSIONS OF LAW

From the Findings of Fact heretofore made and
entered herein, the court here now deduces the fol-
lowing [66]

CONCLUSIONS OF LAW

Defendant is entitled to judgment of dismissal to-
gether with its costs and disbursements as provided
by law.

To the foregoing conclusion of law the plaintiff
excepts and its exception hereby allowed.

Done in open court this 14th day of January,
1935.

District Judge

Presented by:—

Attorney for Defendant

Presented to and refused by the Court Jan. 14, 1935.

JOHN C. BOWEN

Judge."

(Attached to Motion)

"In the District Court of the United States for the Western District of Washington, Northern Division.

No. 20512.

GUY H. CLARK, as Receiver of the Montborne Lumber Company, a corporation,

Plaintiff,

v.

NORTH RIVER INSURANCE COMPANY.

a corporation,

Defendant.

JUDGMENT

This matter coming on regularly to be heard upon application of the defendant, for the entry of judgment herein, the cause having been heretofore tried by the court without a jury on October 3, 1934, upon a stipulation of facts on file herein, and the court, having heretofore filed its memorandum decision herein, and the court having on this 14th day of January, 1935, [67] made and entered its findings of fact and conclusions of law, the plaintiff appearing by his counsel, C. J. Henderson and Alfred McBee, and the defendant appearing by its counsel, Sawyer & Cluff, L. B. daPonte and Robert S. MacFarlane, and the court being fully advised in the premises;

It is therefore ORDERED, ADJUDGED and DECREED that the complaint of the plaintiff

herein be dismissed, and that defendant have and recover of and from the plaintiff its costs and disbursements as provided by law.

Exceptions allowed to plaintiff.

DONE IN OPEN COURT this 14th day of January, 1935.

District Judge

Presented by:—

Attorney for Defendant.

Presented to and refused by the Court, Jan. 14, 1935.

JOHN C. BOWEN

Judge.”

That further on aforesaid January 14, 1935, the said Honorable John C. Bowen made and entered an order denying said motion of the defendant for the entry of Conclusions of Law and Judgment, which order is in words and figures as follows:—

“In the District Court of the United States for the Western District of Washington, Northern Division.

No. 20512

GUY H. CLARK, as Receiver of the Montborne Lumber Company, a corporation,

Plaintiff,

v.

[68]

NORTH RIVER INSURANCE COMPANY,
a corporation,

Defendant.

ORDER.

This matter regularly coming on to be heard be-

fore the undersigned judge of the above entitled court upon motion interposed by plaintiff for the entry of conclusions of law and judgment, and motion interposed by the defendant for the entry of conclusions of law and judgment, and the court being fully advised in the premises,

NOW, THEREFORE, it is

ORDERED that the motion of the plaintiff for the entry of conclusions of law and judgment be and the same hereby is denied, and exception allowed; and it is further

ORDERED that the motion of the defendant for the entry of conclusions of law and judgment be and the same hereby is denied, and exception allowed.

DONE IN OPEN COURT this 14th day of January, 1935.

JOHN C. BOWEN

District Judge

Presented by:—

SAWYER & CLUFF,
L. B. daPONTE,
ROBERT S. MACFARLANE
C. J. HENDERSON,
ALFRED McBEE" [69]

That on the aforesaid 14th day of January, 1935, when the matter of signing Findings of Fact, Conclusions of Law and Judgment came on to be heard

before the court, the plaintiff presented to the court its motion, theretofore served upon the attorneys for the defendant, for entry of conclusions of law and judgment as thereto attached, which said motion and conclusions of law and judgment are in words and figures as follows:—

“In the District Court of the United States for the Western District of Washington, Northern Division.

GUY H. CLARK, as Receiver of the Montborne Lumber Company, a corporation,
Plaintiff,

v.

NORTH RIVER INSURANCE COMPANY,
a corporation,
Defendant.

MOTION FOR THE ENTRY OF CONCLUSIONS OF LAW AND JUDGMENT.

Comes now the Plaintiff and moves the court for the entry of the hereto attached Conclusions of Law and Judgment.

Dated this 14th day of January, 1935.

C. J. HENDERSON

ALFRED McBEE

Attorneys for Plaintiff
Mount Vernon, Washington

Service of copy of the above motion and attached Conclusions of Law and Judgment is hereby

acknowledged this 14th day of January, 1935, by receipt this date of true and correct copies thereof.

SAWYER & CLUFF

L. B. daPONTE

ROBERT S. MACFARLANE

Attorneys for Defendant.

Motion denied, Jan. 14, 1935.

JOHN C. BOWEN,

Judge. [70]

(Attached to Motion)

“In the District Court of the United States for the Western District of Washington, Northern Division.

No. 20512

GUY H. CLARK, as Receiver of the Montborne Lumber Company, a corporation,

Plaintiff,

v.

NORTH RIVER INSURANCE COMPANY,
a corporation,

Defendant.

CONCLUSIONS OF LAW.

From the Findings of Fact heretofore made and entered herein, the court here now deduces the following

CONCLUSIONS OF LAW

Plaintiff is entitled to judgment against the defendant in the sum of FIFTEEN THOUSAND DOLLARS (\$15,000.00), together with interest from the date hereof, together with his costs and disbursements as provided by law.

To the foregoing conclusion of law the defendant excepts and its exception is hereby allowed.

Done in open court this 14th day of January, 1935.

District Judge

Presented by:—

C. J. HENDERSON

ALFRED McBEE,

Attorneys for Plaintiff

Presented to and refused by the Court Jan. 14, 1935.

JOHN C. BOWEN,
Judge." [71]

(Attached to Motion)

"In the District Court of the United States for the Western District of Washington, Northern Division.

No. 20512

GUY H. CLARK, as Receiver of the Montborne Lumber Company, a corporation,
Plaintiff,

v.

NORTH RIVER INSURANCE COMPANY,
a corporation,

Defendant.

JUDGMENT

This matter coming on regularly to be heard upon application of the plaintiff, for the entry of judgment herein, the cause having been heretofore tried by the court without a jury on October 3, 1934, upon a stipulation of facts on file herein, and the

court, having heretofore filed its memorandum decision herein, and the court having on this 14th day of January, 1935 made and entered its findings of fact and conclusions of law, the plaintiff appearing by his counsel, C. J. Henderson and Alfred McBee, and the defendant appearing by its counsel Sawyer and Cluff, L. B. daPonte and Robert S. Macfarlane, and the court being fully advised in the premises:—

It is therefore ordered, adjudged and decreed that the plaintiff do have and recover of and from the defendant the sum of FIFTEEN THOUSAND DOLLARS (\$15,000.00) together with interest at the rate of Six per cent (6%) from the date hereof, together with his costs and disbursements as provided by law.

Exceptions allowed to defendant.

Done in open court this 14th day of January, 1935.

District Judge

Presented by:—

C. J. HENDERSON

ALFRED McBEE

Attorneys for Plaintiff

Presented to and refused by the Court, Jan. 14, 1935.

JOHN C. BOWEN,
Judge." [72]

I, the undersigned United States District Judge, who presided at the trial of the above entitled cause, do hereby certify that the foregoing bill of excep-

tions contains all of the material facts, matters, things, proceedings, rulings, and exceptions thereto, occurring upon the trial of said cause, and not heretofore a part of the record herein, including all evidence adduced at the said trial; and I further certify that the exhibits set forth or referred to, or both, in the foregoing bill of exceptions, constitute all of the exhibits offered in evidence in the said trial, and I hereby make all of said exhibits a part of the foregoing bill of exceptions; and I hereby settle and allow the foregoing bill of exceptions as a full, true, and correct bill of exceptions in this cause and order the same filed as part of the record herein, and further order the clerk of this court to attach to the said bill of exceptions, all of the said exhibits not set forth therein; and to transmit said entire bill of exceptions, including all exhibits whatsoever, to the Circuit Court of Appeals for the Ninth Circuit.

I further certify that the foregoing bill of exceptions contains all orders made by me extending the time and term for the presentation, settling and filing the bill of exceptions, and that the foregoing bill of exceptions is presented, settled and allowed within the time prescribed for that purpose.

Dated this 28 day of January, 1935.

JOHN C. BOWEN

United States District Judge

[Endorsed]: Lodged Jan 16 1935

[Endorsed]: Filed Jan. 28 1935 [73]

[Title of Court and Cause.]

PETITION FOR APPEAL.

To the Honorable John C. Bowen, District Judge:

The above-named defendant, NORTH RIVER INSURANCE COMPANY, a corporation, feeling aggrieved by the judgment made and entered in the above-entitled cause on the 14th day of January, 1935, does hereby appeal from said judgment to the Circuit Court of Appeals for the Ninth Circuit, for the reasons set forth in the Assignment of Errors filed herewith, and it prays that its appeal be allowed and that citation be issued as provided by law and that a transcript of the record, proceedings and documents upon which the said judgment was based, duly authenticated, be sent to the United States Circuit Court of Appeals for the Ninth Circuit, sitting at San Francisco, California, under the rules of such court in such case made and provided.

And your petitioner further prays that upon its giving a bond in an amount to be fixed by this Court, the said appeal may operate as a supersedeas and may suspend, during the pendency of said appeal, execution of said judgment.

DATED: March 1, 1935.

SAWYER & CLUFF

L. B. DaPONTE

ROBERT S. MACFARLANE

Attorneys for Defendant.

[Endorsed]: Filed Mar. 1, 1935 [74]

[Title of Court and Cause.]

ASSIGNMENT OF ERRORS.

North River Insurance Company, a corporation, the defendant herein, asserts that in the record and proceedings in the above-entitled cause, and in the final judgment entered herein, there is manifest error in the following particulars:

FIRST: The Court erred in denying defendant's motion made October 3, 1934, for findings and declaration of law in its favor.

SECOND: The Court erred in denying defendant's motion made January 14, 1935, for the entry, upon the findings, of a conclusion of law that defendant is entitled to judgment of dismissal, together with costs and disbursements as provided by law, and for entry of judgment for defendant pursuant to such conclusion, to which denial defendant duly excepted and its exception was allowed.

THIRD: The Court erred in entering judgment herein for the plaintiff in the sum of Seven Thousand dollars (\$7,000.00) for the reason that the judgment is not supported by the findings, and particularly that portion of Finding No. IV which declares that the locomotive itself was never in contact with the fire and sustained no physical damage as a result of the fire, to the entry of which judgment defendant duly excepted and its exception was allowed.

FOURTH: The Court erred in construing the insurance policy in this case as covering a loss of the insured locomotive when the said locomotive

had suffered no physical damage whatever as a result of the fire or as a result of any other peril insured against.

FIFTH: The Court erred in holding that said locomotive was a total loss by fire within the meaning of said insurance policy.

SIXTH: The Court erred in holding that the fire was the proximate cause of the loss of the locomotive.

SEVENTH: The Court erred in holding that the said locomotive was a total loss by fire.

EIGHTH: The Court erred in holding that the locomotive had sustained any loss or damage whatsoever as a result of fire. [75]

NINTH: The Court erred in construing the insurance policy to cover loss of use of the locomotive.

TENTH: The Court erred in holding the defendant liable upon a contract of insurance for which there was no consideration.

WHEREFORE, said defendant prays that said judgment be reversed and that the District Court be directed by the Circuit Court of Appeals for the Ninth Circuit, to enter a judgment in said cause in favor of said defendant.

DATED Mar. 1, 1935.

SAWYER & CLUFF

L. B. daPONTE

ROBERT S. MACFARLANE

Attorneys for Defendant.

[Endorsed]: Filed Mar. 1, 1935 [76]

[Title of Court and Cause.]

ORDER ALLOWING APPEAL.

On motion of Robert S. Macfarlane, of attorneys for defendant, IT IS HEREBY ORDERED that an appeal to the United States Circuit Court of Appeals for the Ninth Circuit from the judgment heretofore made and entered herein be, and the same is hereby allowed, and that a certified transcript of the record, testimony, exhibits, stipulations, and all proceedings be forthwith transmitted to said Circuit Court of Appeals for the Ninth Circuit.

IT IS FURTHER ORDERED that the bond on appeal be fixed at the sum of Eight thousand Dollars (\$8,000.00), the same to act as a supersedeas bond and also as a bond for costs and damages on appeal.

DATED: March 1, 1935.

JOHN C. BOWEN

District Judge.

[Endorsed]: Filed March 1, 1935 [77]

[Title of Court and Cause.]

SUPERSEDEAS AND COST BOND ON
APPEAL.

KNOW ALL MEN BY THESE PRESENTS:

That we, NORTH RIVER INSURANCE COMPANY, a corporation, as principal, and INDEMNITY INSURANCE COMPANY OF NORTH

AMERICA, a corporation, as surety, are held and firmly bound unto GUY H. CLARK, as Receiver of the Montborne Lumber Company, a corporation, in the full and just sum of Eight thousand Dollars (\$8,000.00), to be paid to the said Guy H. Clark, as Receiver of the Montborne Lumber Company, a corporation, his heirs, executors, administrators and assigns, to which payment well and truly to be made we bind ourselves, our successors and assigns jointly and severally, firmly by these presents.

IN TESTIMONY WHEREOF, North River Insurance Company has caused this instrument to be executed on its behalf and in its name by Ward Jackson, its attorney-in-fact, and said Indemnity Insurance Company of North America has likewise caused this instrument to be executed on its behalf and in its name by Harry C. Miller, its attorney-in-fact, and its corporate seal to be hereon set, all on the 19th day of February, 1935.

WHEREAS, lately at a District Court of the United States for the Western District of Washington, Northern Division, in an action pending in said court between Guy H. Clark, as Receiver of the Montborne Lumber Company, a corporation, as plaintiff, and North River Insurance Company, a corporation, as defendant, a judgment was rendered on the 14th day of January, 1935, against said North River Insurance Company and said North River Insurance Company is about to petition for an allowance of an appeal and file a copy thereof in the Clerk's office of the said court to reverse the

judgment in the said action, and a citation will thereafter be directed to the said Guy H. Clark, as Receiver of the Montborne Lumber Company, a corporation, citing and admonish- [78] ing him to be and appear in the United States Circuit Court of Appeals for the Ninth Circuit, at the City and County of San Francisco, in the State of California, on a day certain to be fixed by the court, and within thirty days from and after the date of said citation.

NOW, the condition of the above obligation is such that if the said North River Insurance Company shall prosecute its said appeal to effect and answer all damages and costs, if it fails to make its plea good, then the above obligation to be void; else to remain in full force and virtue.

NORTH RIVER

INSURANCE COMPANY

By WARD JACKSON

Its Attorney-in-fact

[Seal]

INDEMNITY INSURANCE
COMPANY OF NORTH
AMERICA

By HARRY C. MILLER

Its Attorney-in-fact

Approved March 1, 1935.

JOHN C. BOWEN

Judge of the District Court of the United
States for the Western District of Wash-
ington, Northern Division.

State of California

City and County of San Francisco—ss.

On this 19th day of February, 1935, before me, Lulu P. Loveland, a Notary Public in and for the City and County of San Francisco, State of California, personally appeared WARD JACKSON, known to me to be the person whose name is subscribed to the within instrument as the Attorney-in-fact of NORTH RIVER INSURANCE COMPANY, and acknowledged to me that he subscribed the name of North River Insurance Company thereto as principal, and his own name as Attorney-in-fact.

IN TESTIMONY WHEREOF, I have hereunto set my hand and affixed my official seal, all on the day and year in this certificate first above written.

[Seal]

LULU P. LOVELAND

Notary Public in and for the City and County
of San Francisco, State of California [79]

State of California,

City and County of San Francisco—ss.

On this 19th day of February, 1935, before me, Lulu P. Loveland, a Notary Public in and for the City and County of San Francisco, State of California, personally appeared HARRY C. MILLER, known to me to be the person whose name is subscribed to the within instrument as the Attorney-in-fact of INDEMNITY INSURANCE COMPANY OF NORTH AMERICA, and acknowledged

to me that he subscribed the name of Indemnity Insurance Company of North America thereto as surety, and his own name as Attorney-in-fact.

IN TESTIMONY WHEREOF, I have hereunto set my hand and affixed my official seal, all on the day and year in this certificate first above written.

[Seal]

LULU P. LOVELAND

Notary Public in and for the City and County
of San Francisco, State of California.

[Endorsed]: Filed Mar. 1, 1935 [80]

[Title of Court and Cause.]

PRAECIPE FOR TRANSCRIPT OF RECORD.
TO THE CLERK OF THE ABOVE-ENTITLED
COURT:

You are requested to take a transcript of the record and transmit the same to the United States Circuit Court of Appeals for the Ninth Circuit, omitting all captions and endorsements, verifications, etc., but containing all proofs of service, and to include in such transcript of record the following and no other papers, that is to say:

1. Summons.
2. Complaint.
3. Petition for Removal.
4. Notice of Intention to file Petition and Bond for Removal.
5. Bond on Removal.
6. Order of Removal.

7. Answer.
8. Bill of Exceptions.
9. Assignment of Errors.
10. Petition for Appeal.
11. Order Allowing Appeal and fixing Amount of Cost and Supersedeas Bond.
12. Cost and Supersedeas Bond.
13. Citation and Proof of Service.
14. Praecipe and Proof of Service.
15. Your Certificate.

SAWYER & CLUFF

L. B. daPONTE

ROBERT S. MACFARLANE

Attorneys for Defendant.

We waive the provisions of the Act approved February 13, 1911, and direct that you forward typewritten transcript to the Circuit Court of Appeals for printing as provided under Rule 105 of this court.

C. J. HENDERSON

ALFRED McBEE

Attorneys for Plaintiff.

SAWYER & CLUFF

ROBERT S. MACFARLANE

Attorneys for defendant.

Service hereof admitted this 11 day of March, 1935.

C. J. HENDERSON &

ALFRED McBEE

Attorneys for Plaintiff

[Endorsed]: Filed Mar. 13, 1935 [81]

[Title of Court and Cause.]

CERTIFICATE OF CLERK U. S. DISTRICT
COURT TO TRANSCRIPT ON APPEAL.

United States of America,
Western District of Washington—ss:

I, Edgar M. Lakin, Clerk of the United States District Court for the Western District of Washington, do hereby certify that the foregoing type-written transcript of record, consisting of pages numbered from 1 to 81, inclusive, is a full, true and complete copy of so much of the record, papers and other proceedings in the above and foregoing entitled cause, as is required by praecipe of counsel filed and shown herein, (with the exception of the Summons as requested in said praecipe, none having been included in the transcript on removal from Skagit County to this Court), as the same remain of record and on file in the office of the Clerk of the said District Court at Seattle, and that the same constitute the record on appeal herein from the judgment of said United States District Court for the Western District of Washington to the United States Circuit Court of Appeals for the Ninth Circuit.

I further certify that the following is a true and correct statement of all expenses, costs, fees and charges incurred in my office by or on behalf of the appellant for making record, certificate or return

to the United States Circuit Court of Appeals for the Ninth Circuit, to-wit:

Clerk's fees (Act Feb. 11, 1925) for making record, certificate or return folios at 15c	\$ 34.50
Appeal fee (Sec. 5 of Act)	5.00
Certificate of Clerk to Transcript of Record	.50
Total	40.00

[82]

I hereby certify that the above cost for preparing and certifying record, amounting to \$40.00, has been paid to me by the attorneys for the appellant.

I further certify that I attach hereto and transmit herewith the original citation on appeal issued in this cause.

IN WITNESS WHEREOF I have hereunto set my hand and affixed the official seal of said District Court, at Seattle, in said District, this 29th day of March, 1935.

[Seal] EDGAR M. LAKIN
Clerk United States District Court for the
Western District of Washington,
By TRUMAN EGGER
Deputy. [83]

[Title of Court and Cause.]

CITATION AND NOTICE ON APPEAL

To Guy H. Clark, as Receiver of the Montborne Lumber Company, a corporation, and to Alfred

McBee, Esq., and C. J. Henderson, Esq., attorneys for Guy H. Clark,

GREETING:—

YOU ARE HEREBY NOTIFIED, that in a certain action at law in the District Court of the United States for the Western District of Washington, Northern Division, wherein Guy H. Clark, as Receiver of the Montborne Lumber Company, a corporation, is plaintiff, and North River Insurance Company, a corporation, is defendant, an appeal has been allowed to the defendant therein to the United States Circuit Court of Appeals for the Ninth Circuit.

You are hereby cited and admonished to be and appear in said court at the City and County of San Francisco, State of California, on the 31st day of March next, to do and receive what may appertain to justice to be done in the premises.

Given under my hand at the city of Seattle, in the Ninth Circuit, this 1st day of March in the year of our Lord one thousand nine hundred and thirty-five.

[Seal]

JOHN C. BOWEN

Judge of the District Court of the United States, for the Western District of Washington, Northern Division. [84]

Due service of the within Citation and Notice on Appeal and receipt of copy thereof is hereby admitted and acknowledged on behalf of Guy H. Clark,

as Receiver of the Montborne Lumber Company, a corporation, appellee, this 4 day of March, 1935.

C. J. HENDERSON &

ALFRED McBEE

Attorneys for Appellee.

[Endorsed]: Filed Mar. 13, 1935 [85]

[Endorsed]: No. 7820. United States Circuit Court of Appeals for the Ninth Circuit. North River Insurance Company, a corporation, Appellant, vs. Guy H. Clark, as Receiver of the Montborne Lumber Company, a corporation, Appellee. Transcript of Record. Upon Appeal from the United States District Court for the Western District of Washington, Northern Division.

Filed April 1, 1935.

PAUL P. O'BRIEN

Clerk of the United States Circuit Court of Appeals
for the Ninth Circuit.

[Title of Court and Cause.]

PETITION FOR CROSS APPEAL.

To the Honorable John C. Bowen, District Judge:

The above named plaintiff, Guy H. Clark, as receiver of the Montborne Lumber Company, a corporation, feeling aggrieved by the judgment made and entered in the above entitled cause on the 14th day of January, 1935, does hereby cross appeal from

said judgment to the Circuit Court of Appeals for the Ninth Circuit, for the reasons set forth in cross appellant's assignment of errors filed herewith, and prays that his cross appeal be allowed and that citation be issued as provided by law and that a transcript of the record, proceedings and documents upon which the said judgment was based, duly authenticated, be sent to the United States Circuit Court of Appeals for the Ninth Circuit, sitting at San Francisco, California, under the rules of such court in such case made and provided.

And your petitioner further prays that upon his giving a bond in the amount to be fixed by this court, the said cross appeal may operate as a supersedeas and may suspend, during the pendency of said appeal, execution of said judgment.

DATED this 11th day of April, 1935.

HENDERSON and McBEE

Attorneys for Plaintiff

618 First Street, Mount Vernon, Washington

[Endorsed]: Filed Apr 11 1935 [86]

[Title of Court and Cause.]

CROSS APPELLANT'S ASSIGNMENT OF
ERRORS.

Comes now the plaintiff and cross appellant herein, Guy H. Clark, as receiver of the Montborne Lumber Company, a corporation, and asserts that in the record and proceedings in the above

entitled cause, and in the final judgment herein, there is manifest error in the following particulars:

FIRST: The court erred in denying plaintiff's motion made January 14, 1935, for the entry upon the findings of a conclusion of law that the plaintiff is entitled to judgment against the defendant in the sum of \$15,000.00, together with interest from the date thereof, and with plaintiff's costs and disbursements as provided by law, and for entry of judgment for the plaintiff for said sums pursuant to such conclusion, to which denial plaintiff duly excepted and which exception was regularly allowed.

SECOND: The court erred in construing the insurance policy in this case as not requiring the defendant to pay to the plaintiff \$8000.00, for which the plaintiff was liable to the *North Pacific Railroad*.

THIRD: The court erred in construing the policy of insurance in this case as an indemnity or liability policy instead of a fire insurance policy.

FOURTH: The court erred in holding that the payment by the defendant to the *North Pacific Railroad Company* was an accord and satisfaction of the policy of insurance in this case.

FIFTH: The court erred in holding that the parties to the insurance policy intended that the liability of the insured, rather than the loss or damage to the insured was the thing insured against.

SIXTH: The court erred in holding that as to plaintiff's claimed recovery for damages to the log-

ging flat cars, plaintiff had failed to sustain the burden of proof. [87]

SEVENTH: The court erred in holding that the plaintiff was not legally liable to the railroad company in the sum of \$8000.00.

EIGHTH: The court erred in holding the release and discharge of the plaintiff's predecessor in interest, evidenced by "Exhibit 2", that the plaintiffs wholly failed to prove that as the result of the damage to the cars plaintiff was legally liable to the railroad company in the sum of \$8000.00.

WHEREFORE, plaintiff and cross appellant prays that said judgment be reversed and that the District Court be directed by the Circuit Court of Appeals for the Ninth Circuit, to enter a judgment in favor of the plaintiff and against the defendant in the sum of \$15,000.00 and interest from the 14th day of January, 1935, until paid, and for plaintiff's costs and disbursements herein.

DATED this 11th day of April, 1935.

HENDERSON and McBEE

Attorneys for Plaintiff

618 First Street, Mount Vernon, Washington.

[Endorsed]: Filed Apr 11 1935 [88]

[Title of Court and Cause.]

ORDER ALLOWING CROSS APPEAL.

On Motion of Alfred McBee, one of the attorneys for the plaintiff herein, it is HEREBY

ORDERED that cross appeal to the United States Circuit Court of Appeals for the Ninth Circuit from the judgment heretofore made and entered herein be and the same is hereby allowed, and that a certified transcript of the record, testimony, exhibits, stipulations and all proceedings be forthwith transmitted to the Circuit Court of Appeals for the Ninth Circuit.

IT IS FURTHER ORDERED that the bond on cross appeal to be posted by the plaintiff be and the same is hereby fixed in the sum of \$500.00, the same to act as a bond for costs and damages on cross appeal, and as a supersedeas bond on cross appeal.

DATED this 11th day of April, 1935.

JOHN C. BOWEN

District Judge.

[Endorsed]: Filed Apr 11, 1935 [89]

[Title of Court and Cause.]

COST BOND ON CROSS-APPEAL.

KNOW ALL MEN BY THESE PRESENTS, that We, Guy H. Clark, as receiver of the Montborne Lumber Company, a corporation, as principal, and the **UNITED STATES FIDELITY & GUARANTY COMPANY**, a corporation, as surety, are held and firmly bound unto the North River Insurance Company, a corporation, in the full and just sum of \$500.00 to be paid to the North River In-

insurance Company, a corporation, its successors and assigns, for which payment, well and truly to be made, we bind ourselves, our successors and assigns, jointly and severally, firmly by these presents.

IN TESTIMONY WHEREOF, Guy H. Clark as receiver of the Montborne Lumber Company, a corporation, has executed this instrument and the said United States Fidelity & Guaranty Company, a corporation has likewise caused this instrument to be executed on its behalf and in its name by JOHN C. McCOLLISTER, its attorney in fact, and its corporate seal to be hereon set, all on this 11th day of April, 1935.

The condition of this obligation is such that

WHEREAS, lately at a District Court of the United States for the Western District of Washington, Northern Division, in an action pending therein, between Guy H. Clark, as Receiver of the Montborne Lumber Company, a corporation, as plaintiff, and North River Insurance Company, a corporation, as defendant, a judgment was rendered on the 14th day of January, 1935, wherein the said Guy H. Clark as such receiver was granted judgment against the North River Insurance Company, a corporation, in the sum of \$7000.00, and interest and costs, and

WHEREAS, said judgment also denied recovery to the said Guy H. Clark as receiver aforesaid in the sum of \$8000.00 and

WHEREAS, the said Guy H. Clark, as receiver aforesaid has petitioned for an allowance of a cross

appeal from the said judgment and filed a copy thereof in the office of the clerk [90] of said court to reverse said judgment in said action, and a citation will hereafter be directed to the said North River Insurance Company, a corporation, citing and admonishing it to be and appear in the United States Circuit Court of Appeals for the Ninth Circuit, at the City and County of San Francisco, in the State of California, on a day certain to be fixed by the court, and within thirty days from and after the date of said citation.

NOW, THEREFORE, the condition of this obligation is such that if the said Guy H. Clark, as receiver aforesaid, shall prosecute his said cross appeal to effect and answer all damages and costs, if he fails to make his plea good, then the above obligation to be void, otherwise to remain in full force and effect.

GUY H. CLARK

Receiver of the Montborne Lumber Company,
a corporation

[Seal] UNITED STATES FIDELITY
& GUARANTY COMPANY,
a corporation
By JOHN C. McCOLLISTER

Approved April 11, 1935.

JOHN C. BOWEN

Judge of the District Court of the United
States for the Western District of Wash-
ington, Northern Division. [91]

State of Washington
County of Skagit—ss.

On this 11th day of April, 1935, before me, a Notary Public in and for the State of Washington, County of Skagit, residing at Mount Vernon, Washington, personally appeared GUY H. CLARK, to me known to be the person whose name is subscribed to the within instrument, as the Receiver of the Montborne Lumber Company, a corporation, and acknowledged to me that he subscribed his name as receiver of said corporation for the uses and purposes herein mentioned and described.

IN TESTIMONY WHEREOF, I have hereunto set my hand and affixed my official seal, all on the day and year in this certificate first above written.

[Notary Seal]

ALFRED McBEE

Notary Public in and for the State of Washington, residing at Mount Vernon.

State of Washington
County of

—ss.

On this 11 day of April, 1935, before me, FRANK DRISCOLL, a Notary Public in and for the City of Seattle, County of King, State of Washington, personally appeared John C. McCollister to me known to be the person whose name is subscribed to the within instrument as the attorney in fact of the UNITED STATES FIDELITY & GUARANTY COMPANY, and acknowledged to me that he subscribed the name of the United States Fidelity & Guaranty Company thereto as surety, and his own name as Attorney in fact.

IN TESTIMONY WHEREOF, I have hereunto set my hand and affixed my official seal, all on the day and year in this certificate first above written.

[Notary Seal]

FRANK DRISCOLL

Notary Public in and for the State of Washington, County of King, residing at Seattle, Washington

[Surety Company Seal]

[Endorsed]: Filed Apr 11, 1935 [92]

[Title of Court and Cause.]

ACCEPTANCE OF SERVICE.

Service is hereby accepted and receipt is hereby acknowledged of true and correct copies of the following papers and documents in the above entitled cause:

1. Petition for Cross appeal.
2. Order allowing cross appeal.
3. Praecipe for transcript of record on cross appeal.
4. Cost bond on cross appeal.
5. Cross appellant's assignment of errors.
6. Citation and notice of cross appeal.

SAWYER & CLUFF

L. B. daPONTE

ROBERT S. MACFARLANE

Attorneys for North River Insurance Company,
a corporation.

[Endorsed]: Filed Apr 11 1935 [93]

[Title of Court and Cause.]

**PRAECIPE FOR TRANSCRIPT OF RECORD
ON CROSS APPEAL.**

**TO THE CLERK OF THE ABOVE ENTITLED
COURT:**

You are requested to take a transcript of the record and transmit the same to the United States Circuit Court of Appeals for the Ninth Circuit, omitting all captions and endorsements, verifications, etc., but containing all proofs of service, and to include in such transcript of record the following and no other papers, that is to say:

1. Summons.
2. Complaint.
3. Petition for Removal.
4. Notice of Intention to file Petition and Bond for Removal.
5. Bond on Removal.
6. Order of Removal.
7. Answer.
8. Bill of exceptions.
9. Cross appellant's assignment of errors.
10. Cross appellants Petition for cross appeal.
11. Order allowing cross appeal and fixing amount of cross appellants cost bond.
12. Cross appellant's cost bond.
13. Cross appeallant's Citation.
14. Cross appellant's Praecipe.
15. Cross appellant's acceptance of service (showing acknowledgment of service by appellant.)

16. Your Certificate.

17. Stipulation and Order extending time.

HENDERSON and McBEE

Attorneys for Plaintiff

618 First Street, Mount Vernon, Washington [94]

We waive the provisions of the Act approved February 13, 1911, and direct that you forward typewritten transcript to the Circuit Court of Appeals for printing as provided under Rule 105 of this court.

HENDERSON and McBEE

Attorneys for Plaintiff.

SAWYER & CLUFF

L. B. daPONTE

ROBERT S. MACFARLANE

Attorneys for Defendant.

[Endorsed]: Filed Apr 11, 1935 [95]

[Title of Court and Cause.]

CERTIFICATE OF CLERK U. S. DISTRICT
COURT TO TRANSCRIPT ON CROSS
APPEAL.

United States of America,
Western District of Washington—ss:

I, EDGAR M. LAKIN, Clerk of the United States District Court for the Western District of Washington, do hereby certify that the foregoing typewritten transcript of record on cross appeal,

consisting of pages numbered from 1 to 88, inclusive, is a full, true and complete copy of so much of the record, papers and other proceedings in the above and foregoing entitled cause, as is required by praecipe of counsel filed and shown herein, (with the exception of the Summons as requested in said praecipe, none having been included in the transcript on removal from Skagit County to this Court), as the same remain of record and on file in the office of the Clerk of the said District Court at Seattle, and that the same constitute the record on cross appeal herein from the judgment of said United States District Court for the Western District of Washington to the United States Circuit Court of Appeals for the Ninth Circuit.

I further certify that the following is a true and correct statement of all expenses, costs, fees and charges incurred in my office by or on behalf of the cross appellant for making record, certificate or return to the United States Circuit Court of Appeals for the Ninth Circuit, to-wit:

Clerk's fees (Act Feb. 11, 1925) for making record, certificate or return	230
folios at 15¢	\$ 34.50
Appeal fee (Sec. 5 of Act)	5.00
Certificate of Clerk to Transcript on cross appeal	.50
<hr/>	
Total	\$ 40.00

[96]

I hereby certify that the above cost for preparing and certifying record on cross appeal, amounting

to \$40.00 has been paid to me by the attorneys for the cross appellant.

I further certify that I attach hereto and transmit herewith the original citation on cross appeal issued in this cause.

IN WITNESS WHEREOF I have hereunto set my hand and affixed the official seal of said District Court, at Seattle, in said District, this 17 day of April, 1935.

[Seal]

EDGAR M. LAKIN,

Clerk United States District Court for the
Western District of Washington,

By TRUMAN EGGER

Deputy. [97]

[Title of Court and Cause.]

CITATION AND NOTICE OF CROSS APPEAL

To the North River Insurance Company, a corporation, and to Sawyer and Cluff, and to L. B. daPonte and Robert S. MacFarlane, attorneys for said defendants,

GREETING:

YOU ARE HEREBY NOTIFIED that in a certain action at law in the District Court of the United States for the Western District of Washington, Northern Division, wherein Guy H. Clark, as receiver of the Montborne Lumber Company, a corporation, is plaintiff, and North River Insurance Company, a corporation, is defendant, a cross appeal

has been allowed to the defendant therein to the United States Circuit Court of Appeals for the Ninth Circuit.

You are hereby cited and admonished to be and appear in said court at the City and County of San Francisco, State of California, on the 9th day of May next, to do and receive what may appertain to justice to be done in the premises.

Given under my hand at the city of Seattle, in the Ninth Circuit, this 11th day of April in the year of our Lord one thousand nine hundred and thirty-five.

[Seal]

JOHN C. BOWEN

Judge of the District Court of the United States, for the Western District of Washington, Northern Division.

[Endorsed]: Filed Apr 11 1935 [98]

[Title of Court and Cause.]

STIPULATION

IT IS HEREBY STIPULATED by and between the parties hereto, by their respective counsel undersigned, that all papers in connection with the appeal and cross appeal of the above entitled cause may be printed under one cover and that it shall not be necessary to print in the cross-appellant's transcript of record any papers, documents or exhibits which are printed in the appellant's transcript of record, and that it shall only be neces-

sary to print in cross appellant's transcript of record the following papers:

1. Cross appellant's petition for cross appeal.
2. Order allowing cross appeal.
3. Cross appellant's citation and notice of appeal.
4. Cross appellant's appeal bond.
5. Cross appellant's assignment of errors.

and such others in connection with the cross appeal as may seem to the Clerk of the Circuit Court of Appeals necessary to perfect cross appellant's appeal.

DATED this 25th day of April, 1935.

HENDERSON & McBEE

Attorneys for Cross Appellant

L. B. da PONTE

ROBERT S. MACFARLANE

SAWYER & CLUFF

Attorneys for Appellant

SO ORDERED:

CURTIS D. WILBUR

Senior U. S. Circuit Judge.

[Endorsed]: Certified Transcript upon cross-appeal. Filed April 19, 1935.

PAUL P. O'BRIEN

Clerk [99]

2
No. 7820

IN THE
United States Circuit Court of Appeals
For the Ninth Circuit

NORTH RIVER INSURANCE COMPANY

(a corporation),

Appellant and Cross-Appellee,

vs.

GUY H. CLARK, as Receiver of the Mont-
borne Lumber Company (a corpora-
tion),

Appellee and Cross-Appellant.

BRIEF FOR APPELLANT AND CROSS-APPELLEE.

HAROLD M. SAWYER,

Balfour Building, San Francisco, California,

L. B. DA PONTE,

ROBERT S. MACFARLANE,

Smith Tower, Seattle, Washington,

*Attorneys for Appellant
and Cross-Appellee.*

FILED

JUL 25 1935

PAUL F. O'BRIEN,

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No. 7820

IN THE
United States Circuit Court of Appeals
For the Ninth Circuit

NORTH RIVER INSURANCE COMPANY

(a corporation),

Appellant and Cross-Appellee,

vs.

GUY H. CLARK, as Receiver of the Mont-
borne Lumber Company (a corpora-
tion),

Appellee and Cross-Appellant.

BRIEF FOR APPELLANT AND CROSS-APPELLEE.

This appeal is taken from a judgment of the District Court of the United States for the Western District of Washington, Northern Division, awarding to appellee and cross-appellant the sum of seven thousand dollars (\$7000.00) as and for a total loss by fire of a certain logging locomotive owned by appellee and cross-appellant and insured against loss or damage by fire and certain other perils by appellant and cross-appellee.

For simplicity, we shall hereafter refer to appellant and cross-appellee as defendant, and appellee and

cross-appellant as plaintiff, which are the positions they respectively occupied in the Court below.

The plaintiff is the receiver of the Montborne Lumber Company, which owned the locomotive, and the defendant is an insurance company. The plaintiff commenced an action on the policy against defendant in the Superior Court of the State of Washington, in and for the County of Skagit, from which defendant removed the case to the District Court of the United States for the Western District of Washington, Northern Division. Thereafter, issue was joined and the case was tried to the Court without a jury, upon a stipulation of facts. The attorneys for the respective parties then made motions for a declaration of law and for special findings in accordance with the said stipulation, and for judgment in favor of their respective clients (Tr. 57). Findings of fact by the Court were made in the precise language of the stipulations of facts (Tr. 65). Judgment was given for the plaintiff in the sum of seven thousand dollars (\$7000.00), from which judgment this appeal is prosecuted.

STATEMENT OF FACTS.

On August 11, 1930, Montborne Lumber Company was engaged in the business of logging near Montborne, Skagit County, Washington, and in connection with said operations the lumber company built a logging railroad partly over trestles, back into the timber to the scene of the logging operations from the station of Montborne on the Seattle-Sumas main line of the Northern Pacific Railway Company (Tr.

33, Par. 3). The lumber company owned a certain ninety (90) ton Shay locomotive, shop number 2703 (Tr. 34, Par. 5). The cars used in the logging operations were not owned by the lumber company but were furnished by the Northern Pacific Railway Company and were hauled to and from Montborne station by the logging engine. These cars were delivered by the railway company under an agreement commonly used in such operations, by the terms of which the lumber company became, to all intents and purposes, an insurer of the rolling stock belonging to the railway company (Tr. 34-35, Pars. 6, 7 and 8; Tr. 40, Par. 2).

On August 11, 1930, the defendant insurance company issued to the Montborne Lumber Company its policy of insurance which insured the logging locomotive against various perils, including that of fire (Tr. 50, Par. 2), which by endorsement of the same date (Tr. 56), insured the legal liability of the logging company with respect to the rolling stock belonging to the Northern Pacific Railway Company.

About September 4, 1930, a forest fire broke out in the holdings of the lumber company and spread on to and over portions of the logging railroad, destroying the bridges and trestles of the railroad (Tr. 34, Par. 4). The fire also damaged a number of cars belonging to the Northern Pacific Railway Company (Tr. 36, Par. 11). The logging locomotive, however, was then situated on the logging railway in the woods, and by reason of the destruction of the bridges and trestles on the logging railroad between the locomotive and Montborne station, the locomotive was marooned. The locomotive itself was never in contact

with the fire and sustained no physical damage as a result of the fire (Tr. 34, Par. 5). The cost of sufficiently repairing the bridges and trestles in order to get the locomotive out of the woods down to Montborne station would exceed the value of the locomotive, which is agreed to be seven thousand dollars (\$7000.00), (Tr. 34, Par. 5).

The defendant insurance company, which had insured the legal liability of the lumber company with respect to the Northern Pacific Railway Company cars, paid eight thousand dollars (\$8000.00), the value of the damaged cars directly to the Northern Pacific Railway Company (Tr. 38, Par. 17), under an agreement wherein the railway company undertook to save the insurance company harmless from any claim at the hands of anyone with respect to these cars. The insurance company refused to pay anything for the locomotive (Tr. 38, Par. 18).

Suit was brought upon the policy by the receiver of the Montborne Lumber Company for the purpose of recovering seven thousand dollars (\$7000.00), the agreed value of the locomotive, and also the amount of money which the insurance company had previously paid to the Northern Pacific Railway Company (Tr. 39, Par. 19).

Judgment was rendered for the plaintiff for the agreed value of the locomotive, seven thousand dollars (\$7000.00), and the claim for the lost and damaged railway cars was disallowed (Tr. 31).

This appeal is from the judgment awarding the plaintiff seven thousand dollars (\$7000.00) for the

locomotive and the cross-appeal is from that portion of the judgment denying the plaintiff the value of the lost and damaged railway cars. This brief will concern itself only with the judgment for the value of the locomotive. The Northern Pacific Railway Company, although not a party to the litigation in form, is in reality defending through its own counsel the claim for the lost and damaged railway cars and will write the brief in the cross-appeal.

ASSIGNMENT OF ERRORS.

The assignment of errors is as follows:

First: The Court erred in denying defendant's motion made October 3, 1934, for findings and declaration of law in its favor.

Second: The Court erred in denying defendant's motion made January 14, 1935, for the entry, upon the findings, of a conclusion of law that defendant is entitled to judgment of dismissal, together with costs and disbursements as provided by law, and for entry of judgment for defendant pursuant to such conclusion, to which denial defendant duly excepted and its exception was allowed.

Third: The Court erred in entering judgment herein for the plaintiff in the sum of seven thousand dollars (\$7000.00), for the reason that the judgment is not supported by the findings, and particularly that portion of Finding No. IV which declares that the locomotive itself was never in contact with the fire and sustained no physical damage as a result of the fire, to

the entry of which judgment defendant duly excepted and its exception was allowed.

Fourth: The Court erred in construing the insurance policy in this case as covering a loss of the insured locomotive when the said locomotive had suffered no physical damage whatever as a result of the fire or as a result of any other peril insured against.

Fifth: The Court erred in holding that said locomotive was a total loss by fire within the meaning of said insurance policy.

Sixth: The Court erred in holding that the fire was the proximate cause of the loss of the locomotive.

Seventh: The Court erred in holding that the said locomotive was a total loss by fire.

Eighth: The Court erred in holding that the locomotive had sustained any loss or damage whatsoever as a result of fire.

Ninth: The Court erred in construing the insurance policy to cover loss of use of the locomotive.

Tenth: The Court erred in holding the defendant liable upon a contract of insurance for which there was no consideration (Tr. 102-103).

These assignments may be grouped and will be discussed under the following affirmative propositions:

1. Inasmuch as the stipulation of facts and the finding made thereon is that the locomotive itself was never in contact with the fire and sustained no physical damage as a result of the fire, it was error to hold that the locomotive had sus-

tained any loss or damage whatever as a result of fire within the meaning of the insurance policy.

2. The judgment in effect permits plaintiff to recover for a loss of use of the locomotive under an insurance policy which did not insure such loss of use and for which the plaintiff paid no consideration.

3. Fire was not the proximate cause of the loss, if any, of the locomotive.

ARGUMENT.

I.

INASMUCH AS THE STIPULATION OF FACTS AND THE FINDING MADE THEREON IS THAT THE LOCOMOTIVE ITSELF WAS NEVER IN CONTACT WITH THE FIRE AND SUSTAINED NO PHYSICAL DAMAGE AS A RESULT OF THE FIRE, IT WAS ERROR TO HOLD THAT THE LOCOMOTIVE HAD SUSTAINED ANY LOSS OR DAMAGE WHATSOEVER AS A RESULT OF FIRE WITHIN THE MEANING OF THE INSURANCE POLICY.

It was expressly stipulated that

“The locomotive itself was never in contact with the fire and sustained no physical damage as a result of the fire” (Tr. 34, Par. 5).

and the finding made by the court was in exact accord with the stipulated fact (Tr. 75; Finding No. IV). Nevertheless, the Court gave judgment for the full agreed value of the locomotive as and for a total loss by fire.

This, we claim, was manifest error. The error is intended to be raised by the first, second, third, fourth,

fifth, seventh and eighth assignments of error (Tr. 102-103).

This action is founded upon a policy of insurance which insured not only against fire but derailment, collision, as defined in the policy, collapse of bridges, lightning, cyclone, tornado and flood (Tr. 50, Par. 2). The only peril relied upon by the plaintiff was fire, and yet recovery was permitted in spite of the fact that the locomotive suffered no physical damage whatsoever and was, after the fire, just as perfect in form and function as it was before. This is an astounding result and one that the parties to the contract of insurance never contemplated at the time it was written.

It can be seen from a mere reading of the policy that the subject matter of the insurance is a locomotive and that what the parties contemplated when the contract of insurance was written was a loss of or damage to the locomotive in the sense that it should either be totally destroyed by fire so that it bore no resemblance to the operative machine described as a locomotive, or else that it should be so physically damaged that it required physical repair.

The perils clause itself shows an intention to insure against risks which, if operative, might reduce the locomotive to a disorganized collection of mechanical parts or damage it so that it could not operate as a locomotive. Among the perils are not only fire but derailment or collision, in which events it must be obvious that there would be physical loss or damage to the locomotive. The other perils are collapse of

bridges, lightning, cyclone, tornado and flood, all of which, if operative, would result in physical loss or damage to the locomotive.

This understanding of the parties is reinforced by the language of two clauses in the policy, both of which contemplate physical loss or damage to the locomotive. The second paragraph under clause 2, Perils Insured Against, reads as follows (Tr. 51):

“It is understood and agreed that in the event of *loss or damage to any part or parts* of the within insured property resulting from any one accident from perils insured against, this company shall only be liable for loss or damage in excess of two hundred fifty dollars (\$250.00).”

Again in paragraph 3-c of the policy (Tr. 51), we find the following significant language:

“It is mutually understood and agreed that this company shall not be liable beyond the actual cash value of the interest of the assured in the property at the time of loss or damage nor *exceeding what it then cost the assured to repair or replace the same with material of like kind and quality.*”

It thus clearly appears from the language of the policy itself that the liability contemplated is for the physical damage to the locomotive from a peril insured against.

The Court below justified its judgment upon the theory “that the value of the locomotive itself has been as effectually destroyed by the destruction of the bridges and consequent marooning of the locomotive as if the fire had reduced to a molten mass the com-

ponent materials of the locomotive" (Opin. of the Court, Tr. 61, last par.).

The destruction of the trestles and the finding that their reconstruction would exceed the value of the locomotive (Finding No. IV; Tr. 75), are false quantities in the case. This conclusion can be tested in very simple fashion. Suppose there was only one bridge between the terminus of the railway in the woods and its junction with the main line of the Northern Pacific; that the bridge collapsed from the weight of a car on it at a time when the locomotive was at the terminus of the logging road in the woods, and that the cost of repairing the bridge was, say, \$500.00. Assume further that the bridge would have to be repaired in order to conduct the operations of the logging company. Could anyone say that the cost of repairs to the bridge would be a claim under a policy insuring the locomotive which, according to hypothesis, has received no physical damage of any kind?

Or suppose that a flood (a peril insured against, policy clause 2, Tr. 67) washed out fifty feet of track while the locomotive was at the terminus in the woods. Could it be said that the cost of repairing the track was a claim under this policy which insures the locomotive and not the track? The mere statement of the question carries with it its own answer, which of course obviously is a negative one. It follows, therefore, that the cost of repairing the track or the expense of rebuilding bridges, whether more or less than the value of the locomotive, cannot possibly be a factor in the case, and that the finding of the Court

to the effect that the cost of sufficiently repairing the said bridges and trestles in order to get the locomotive out of the woods and down to Montborne station would exceed the value of the locomotive can furnish no possible support for the judgment.

In this connection we call the attention of the Court to a very recent case, *Weinberger Banana Co. vs. Phoenix Assurance Co.*, 74 Fed. (2d) 539, (5 C.C.A.). In this case it was held that the insured could not recover for loss of bananas due to delay of a train transporting bananas because of washed out bridges, under a policy insuring against loss of bananas by reason of accident to conveyance during transportation. The following language from the opinion of the Court is peculiarly applicable to the situation presented by the case at bar. We quote as follows:

“If the parties to the contract had intended the insurance of the bananas to cover, in addition to the risk of derailment, collision and other named risks, also risks of accident not only to the car or cars on which the bananas were loaded but to railroad tracks or bridges and railroad equipment other than cars, it may fairly be inferred that appellant would not have tendered, and appellee would not have accepted, a policy containing a typewritten rider specifying the risks insured against in which no accident affecting the safety of the bananas was mentioned except by the use of the words ‘any accident to the conveyance’. If risks of accidents other than such as might happen to the car or cars upon which the bananas were loaded had been intended to be insured against, it reasonably may be supposed that the

typewritten rider, which enumerated the risks insured against while the bananas were on hand, would have contained instead of the words ‘any accident to the conveyance’ some such language as ‘any accident to the track, bridges, cars, or other railroad equipment causing loss or damage to the bananas’, or ‘any accident resulting in loss or damage to the bananas while loaded on railroad cars’ ” (pp. 541-542; italics ours).

Suppose again the locomotive could be used only for hauling lumber and that on account of its peculiar construction it could be used only for hauling logs in the district where the fire occurred, or suppose that the fire destroyed all the timber that could be logged, and further, that at the time of the fire the locomotive was safe at Montborne station. According to plaintiff’s theory there would be a loss under the policy because the locomotive had lost its employment.

Or suppose that a portion of the track between the woods and Montborne station was owned by the Northern Pacific instead of the lumber company, and that this track was destroyed by fire so that the locomotive was just as much marooned in the woods as it is now, and suppose, further, that for some reason or other the Northern Pacific did not care to rebuild the track or did not do so for a year. Under the plaintiff’s theory, if the track were never rebuilt by the Northern Pacific there would be a total loss of the locomotive, and if it were rebuilt within a year there would be a partial loss, in which case we would be pleased to know how the plaintiff would calculate its loss.

All of these supposititious cases demonstrate very clearly that at the time this policy was written, the parties contemplated nothing but physical loss of or damage to the locomotive. After all, an insurance contract must, like any other contract, be interpreted in the light of the intention of the parties.

As was said in the case of *King vs. New York Life Insurance Co.*, 72 Fed. (2d) 620 at 623:

“Courts should not be cunning and astute to evade rather than quick to perceive and diligent to apply, the meaning of the words, as manifestly intended by the parties.”

In the Court below, the plaintiff took the position that ignition or burning of the subject matter of the insurance was not necessary to justify a recovery for loss or damage under a fire policy. This is, of course, undoubtedly true and the books abound with examples of cases where, under a fire policy, the plaintiff was permitted to recover even though there was no ignition or burning. A familiar example for which no authority need be cited is the case of destruction of goods by water used to extinguish a fire, but in these cases and all of the cases relied upon by plaintiff there was *the element of physical destruction or damage*.

Take the cases of *Russell vs. German Fire Insurance Co.* (Minn.), 10 L. R. A. (N. S.) 326; 111 N. W. 400, and *Western Assurance Co. vs. Hann* (1917), 201 Ala. 376; 78 So. 232. These are known as fallen wall or building cases, and in both of them there was serious physical loss and damage. Furthermore, in each there was a question of fact as to whether the antece-

dent fire which damaged and weakened the wall, or the subsequent wind which blew it over, was the proximate cause. This question is obviously one of fact for a jury, and all these cases hold is that the jury's finding under the circumstances will not be upset.

Again, in *Brandyce vs. U. S. Lloyd's, Inc.* (N. Y. 1924), 147 N. E. 201, there was the element of physical loss and damage in that the potatoes physically deteriorated and were sold in damaged condition for about sixty per cent of their sound value. In this case the peril insured against was sea peril, which obliged the vessel with the potatoes on board to seek a port of refuge and the deterioration took place during delay in the port of refuge. The significant point is that there was physical damage and deterioration of the potatoes.

In *Hall vs. Great American Ins. Co.* (Iowa, 1934), 252 N. E. 763, there was this ever present element of physical loss and damage in that the ring involved in that case could not be found after the fire. But observe again, as in the fallen wall cases, the question of what happened to the ring, or in other words, the proximate cause of its loss, was a question of fact which was properly left to the jury. The holding of the case is in reality that the finding of the jury that the ring was lost by fire, or as a result of fire, will not be disturbed. Once more, however, be it observed that there was a physical loss of the ring. The locomotive has not been lost but is in the woods in as good condition as it was before the fire.

In *Lynn Gas & Electric Co. vs. Meriden Fire Ins. Co.*, 158 Mass. 570; 33 N. E. 690; 20 L. R. A. 297, there was again this indispensable element of physical damage. All the case holds is that notwithstanding the intricate chain of causation, this physical loss and damage was proximately caused by the fire.

In *Stag Mining Co. vs. Missouri Fidelity Co.* (Mo. 1919), 209 S. W. 321, there was not only physical loss but the liability was admitted by the insurer. The only question in the case was the measure of indemnity and whether it should be what the land sold for under execution, or what it was really worth.

This also was substantially the question in *Brady vs. Northwestern Assurance Co.*, 11 Mich. 425. There was no question of proximate cause in this case but only of the measure of indemnity, whether it should be the full value of a building partially destroyed by fire which, under a local ordinance could not be repaired, or merely the value of the materials destroyed.

In any event, the *Brady* case is entirely distinguishable. In the first place, it presents the element which is ever present in plaintiff's authorities and totally lacking in the case at bar, namely, that of physical loss and damage. In the second place, it goes upon the ground that the existence of the ordinance was, or should have been, known to the underwriters and therefore the precise situation which arose in the *Brady* case must have been within the contemplation of the parties. As we have already shown, it was never in the contemplation of the parties, nor the intention of either, as derived from the language of the

insurance policy, that the underwriter should be liable in the event of a forest fire which did no physical damage to the locomotive.

In *Hale vs. Washington Ins. Co.*, 11 Fed. Cas. No. 5916, there was also a physical loss, namely, the amount of money which the owner of the insured vessel was obliged to pay to the British vessel as a result of the collision, which was a risk insured against in the policy on the American vessel. There can be no question of the correctness of this decision. This expenditure which the assured was allowed to recover under his policy was a compulsory one. There is, however, no element of compulsion in the case at bar. The plaintiff is not obliged to rebuild the tracks and trestles, and in no true sense can the locomotive be said to be chargeable with the expense of such reconstruction.

The foregoing were the authorities relied upon by plaintiff in the Court below. None, however, are in point in the determination of the question at bar because in every one of these cases there was a recovery for physical loss and damage.

The circumstance that notwithstanding diligent search, plaintiff's counsel has been unable to find a single case in which recovery against an underwriter on this type of policy has been allowed where there was no element of physical loss or damage, should be persuasive in reaching the conclusion that policies of this type insure nothing but physical loss or damage arising from perils insured against.

On the other hand, we are able to present to the Court a case in which a specific object was insured

against designated perils and in which there was a financial loss, but because there was no physical damage to the insured object, recovery was denied. The case is *Edgar Thompson Steel Co. vs. Boylston Mutual Ins. Co.*, 12 Mo. App. 244. In this case the plaintiff insured pig iron on a policy of marine insurance against several perils, including sea peril. The subject matter of the insurance was pig iron in transit. The iron was loaded on a barge and the barge sank in the Mississippi. The underwriter recovered the pig iron from the river and sent it to destination, where it arrived undamaged. The plaintiff brought suit on the policy upon the ground that had there been no accident, the iron would have reached the port of Pittsburgh on the eighth day of March, 1880, at which time it was worth \$43.00 per ton, but was worth a considerably lesser sum when it actually did arrive. Judgment went against the plaintiff. In the course of the opinion the Court said:

“It is evident on a reading of the petition that the plaintiff does not claim insurance for loss of its property * * *.

So, * * * it is safe to say that insurance against injury, detriment or damage to goods caused by the perils of navigation will secure no indemnity against losses from delay caused by the same perils not involving any injury, detriment or damage to the goods * * *. A loss in value consequent upon the falling market, combined with delay in transportation, is due in part, at least, to something else beside the causes specified in the guarantee. It results also from the fluctuations of commerce, which have nothing to do with the perils of navigation.

* * * The entire guarantee, in short, is that the goods shall arrive whole and uninjured at Bessemer. * * * We cannot see from the showing in the petition that the insurers were in any default upon the terms of their engagement.”

It will be noted that in this case, as in the case at bar, the plaintiff suffered a loss but there was no physical damage to the goods. It could well be argued that there was a loss by sea peril. The iron, however, arrived in undamaged condition, just as the locomotive in the woods is in undamaged condition. The Court says that the engagement of the underwriters was that it should arrive in undamaged condition, and in the case at bar the engagement of the underwriters is that the locomotive shall not be physically lost or damaged by fire.

In the Court below, plaintiff's counsel pointed out that the underwriters in the pig iron case fished the pig iron out of the water and sent it on to destination and that under the authority of this case the underwriter in the case at bar should rebuild the tracks and trestles and get the locomotive out, if it did not wish to pay the value of the locomotive. It was said that figuratively speaking the locomotive was at the bottom of the river just as much as the pig iron was.

This reasoning is entirely fallacious and overlooks completely the distinction between the policy in the case of the pig iron and the policy in the case at bar. The obligation of underwriters on a policy insuring goods in transit from A to B is that the goods shall arrive at B undamaged by reason of the operation of

any peril insured against. In the case at bar there is no such transit obligation. *There is no guarantee or insurance that the locomotive shall run during the life of the policy upon the tracks between the woods and Montborne station, or that it shall run at all.* The only insurance is that during the life of the policy the locomotive shall not be physically lost or damaged by reason of fire.

II.

THE JUDGMENT IN EFFECT PERMITS PLAINTIFF TO RECOVER FOR A LOSS OF USE OF THE LOCOMOTIVE UNDER AN INSURANCE POLICY WHICH DID NOT INSURE SUCH LOSS OF USE AND FOR WHICH THE PLAINTIFF PAID NO CONSIDERATION.

This point is raised by the ninth and tenth assignment of errors (Tr. 103).

What the plaintiff has lost is an opportunity to make profitable use of the locomotive unless, of course, it is willing to go to the expense of rebuilding the track and trestles. The locomotive itself is undamaged and not one single one of its functions has been impaired. It is a going concern but limited in its operation solely because of the lack of track and trestles. The track and trestles were not insured under this policy. Neither was the mechanical and useful operation of the locomotive insured. What the plaintiff, therefore, is in reality seeking is to read into a fire policy which specifically insures the locomotive, an insurance of some gain, actual or prospective, to arise from dealing with the locomotive.

This is a subject matter of insurance which can, of course, be covered by a proper policy. It is very closely analogous to a policy of use and occupancy or to one on profits. An insurance of this character, however, cannot be read into a policy which insures specific objects against designated perils.

In *Leonarda vs. Phoenix Ins. Co. of London*, 15 La. Rep. (part 2) 71; 2 Rob. 131, the plaintiff sued upon a fire policy claiming a loss of rent while repairs to the building were being made. In giving judgment for the underwriters the Court said:

“There is much analogy between the rent of a house and the freight of a ship; both are the civil fruits of the thing from which they are derived. It is believed that the attempt has never been made to recover freight under a policy of insurance on a vessel; and yet the loss of the freight, like that of the rent, is a direct consequence of the destruction of the vessel. In both cases the loss falls on a thing which is no part of the object insured and which is not, therefore, covered by the policy.”

Suppose an oil burning steamer was in an out of the way port to fuel and that as a result of conflagration the fuel supply of the entire port was destroyed so that the steamer, for lack of fuel, was unable to arrive at a distant loading port in time to enable her to fulfill a valuable charter, with the result that a substantial profit was lost. Fire undoubtedly is the agency that deprives the steamer of her profit and causes a loss. If the hull policy covered the risk of fire, could anyone say that under these circumstances the under-

writers who insured the steamer and not the charter would be liable for this loss?

A case arose in England in which the assured had taken the policy upon his interest only in the Ship Inn. An arbitrator awarded him a sum for loss sustained his business as an innkeeper, the inn having been partially destroyed by fire, but Lord Denman, C. J., said:

“It is clear to us that the arbitrator had no authority to award compensation to Wright for the loss he had sustained in his business by not being able to occupy the premises. The policy was not intended to cover profits of the business.

Littledale, J. I am of the same opinion.

Taunton, J. I think that profits are insurable but they must be insured as profits. A party is not entitled to compensation for loss of profits under an insurance of his interest in the Ship Inn.”

(*In re Sun Fire Office*, 3 N. & M. 819, Court of King’s Bench, 1835).

In *Stock vs. Engels*, L. R. 9 Q. B. D. (1881-2) 708, plaintiff had effected a policy of marine insurance on goods and made a contract to buy sugar from a merchant. The merchant put a quantity of sugar on a vessel but no selection in a technical sense was ever made of any particular sugar. A loss having occurred, it was held that the plaintiff had no insurable interest in the sugar but that he did have an insurable interest in the profits. It was held, however, that the profits had not been insured, the object of the insurance being the goods. The Court said:

“Whether the profit was lost by any of the perils insured against, it is unnecessary for me to consider, for it is now well settled that such a loss cannot be recovered under a policy framed like the present, merely on goods.”

Perhaps the strongest language as to the necessity of insuring profits specifically is to be found in *Lusena vs. Craufurd*, 127 Eng. Rep. 630 at 648, where the reporter says:

“The learned judges were unanimously of the opinion that the policy in question could not be considered as a policy on profits, having been expressly declared a policy upon the plaintiff’s interest in the ship and goods themselves; and that if it had been intended as a policy on profits, it should have been so stated.”

An American expression of this same opinion is to be found in *Connecticut Fire Ins. Co. vs. W. H. Roberts Lumber Co.*, 119 Va. 479; 89 S. E. 945, where the Court said:

“The character of contracts of insurance of property or an interest or interests in the property itself is very different from a contract of insurance of profits to arise from dealing with such property * * * and the text writers and decisions of the courts seem to be uniform in their expression of the rule that a policy of insurance will not be held to cover profits unless the purpose to do so is expressly stated in the policy.”

At first blush it might appear that the profits cases cited above throw little light on the subject of this inquiry, but when the precise nature of the plaintiff’s

loss is considered, it becomes apparent that the profits cases in reality furnish the clue for which we are looking.

These cases on profits show, to our mind, conclusively that the plaintiff is endeavoring to read into the policy a form of insurance which is not in the policy under the settled canons of insurance law and was certainly never contemplated by the parties at the time the contract was made. Moreover, the plaintiff paid no premium for this extraordinary form of protection which he has now capitalized in the shape of a judgment.

III.

FIRE WAS NOT THE PROXIMATE CAUSE OF THE LOSS, IF ANY, OF THE LOCOMOTIVE.

This point is raised by the sixth assignment of errors (Tr. 103).

In the Court below the plaintiff relied upon general expressions of the rule of proximate cause found in the text writers and similar definitions appearing in the authorities which we have heretofore analyzed under point I of this brief. These definitions, however, are all derived from actual decided cases in which there was physical loss or damage to the specific subject matter of the insurance, and the plaintiff has not been able to present a single case in which recovery was allowed, notwithstanding the fact that the subject matter of the insurance was as perfect in form and function as it was before the fire.

Nothing is better settled than the principle that general expressions and definitions in broad terms must be confined to the circumstances to which they have reference or have been applied. In *Bird vs. St. Paul Fire & Marine Ins. Co.*, 224 N. Y. 47; 13 A. L. R. 875; 120 N. E. 86, the Court, speaking by Cardozo, J., (now Associate Justice of the Supreme Court of the United States), said:

“General definitions of a proximate cause give little aid. Our guide is the reasonable expectation and purpose of the ordinary business man when making an ordinary business contract.”

Again, in *Leyland Shipping Co. vs. Norwich Union Fire Ins. Society*, 1918 A. C. 350, 369, Lord Shaw, of the House of Lords, used the following language:

“The true and the overruling principle is to look at a contract as a whole and to ascertain what the parties to it really meant. What was it which brought about the loss, the event, the calamity, the accident, and this, not in an artificial sense, but in that real sense which parties to a contract must have had in their minds when they spoke of cause at all.”

After all, an insurance contract must, like any other contract, be interpreted in the light of the intention of the parties. The several supposititious cases put under the first point of this argument, clearly demonstrate that the parties to this insurance contract never contemplated anything but physical loss and damage to the locomotive. To allow the plaintiff to recover in this action is to put a premium upon the cunning and astute evasion condemned in *King vs. New York*

Ins. Co. supra; it is to deal with causation in the “artificial sense” that Lord Shaw had in mind in the *Leyland Shipping* case, and not in the “real sense which parties to a contract must have had in their minds when they spoke of cause at all.”

As a matter of fact, the fire is not the proximate cause of the loss of which the plaintiff complains, namely, his inability to use the engine. The finding that the cost of sufficiently repairing the bridges and trestles in order to get the locomotive out of the woods and down to Montborne station would exceed the value of the locomotive (Tr. 75, Finding No. IV), and the finding that shortly after the fire the lumber company became hopelessly insolvent and went into receivership and is now being liquidated (Tr. 81, Finding No. XIII), show very clearly two things: First, that the plaintiff has no further productive use for the locomotive, as the logging operations are to be abandoned, and second, that it will cost more to get the locomotive out than it is worth.

Now, suppose the plaintiff was entirely solvent and still had an abundant supply of timber from the logging of which it could derive profits far in excess of the relatively small cost of rebuilding the railroad and trestles. Obviously it would rebuild and that, too, without regard to the comparatively small value of the locomotive as compared with the cost of rebuilding. Under such circumstances, would anyone say that the whole, or any part, of the cost of rebuilding the railroad should be collected from the underwriters who insured the locomotive against the risk of physical loss or damage by fire?

This illustration shows, we think, that there has been no loss whatever of the locomotive. If the railroad were rebuilt, the locomotive would be just as valuable as ever and there would be no loss whatever. How, then, can the fact that it is not economically desirable, owing to plaintiff's insolvency and liquidation, to rebuild the railroad and trestles, convert an absolutely sound physical engine into a total loss, or any loss at all?

The underwriter in this case never insured the railroad or the trestles or agreed directly or indirectly that they should continue in existence during the life of the policy. The Court below, however, has held in effect that if it is not economically desirable to rebuild the railroad, the owner of the railroad has sustained a total loss of its locomotive even though that locomotive is physically as good as it was before the fire.

We submit that any interpretation of proximate cause which produces such a result is artificial and cunning in the extreme.

CONCLUSION.

This is a case of first impression. The industry and research of counsel for both parties has not succeeded in producing any controlling authority. The principle which should govern the decision in this case has to be spelled out from cases which are at best analogous. The facts in this case are novel, but this novelty should not obscure the principles involved. It is one of the virtues of the common law that it has the

capacity to meet new situations as they arise and deal with them in the light of established principles.

We take it that the principles involved in a decision of this case are, first, that any contract, insurance or otherwise, should be construed in the light of the intention of the parties and the situation which they contemplated at the time the contract was made; second, that the question of proximate cause should be dealt with in a realistic and not an artificial sense; and third, that while the benefits to be derived from the use of property may be insured, they are not insured under a policy on the property itself.

We have shown that no one at the time this contract of insurance was made contemplated protection against anything except physical loss and damage to the locomotive and that certainly the parties never had in mind a case where a raging forest fire would spread destruction over a large area and leave the locomotive untouched. We have also shown that in no realistic sense has there been any loss of or damage to the locomotive in any degree whatsoever as a result of fire but solely because, for one reason or another, the railroad has not been rebuilt, and we have shown that the plaintiff is endeavoring to utilize this policy as a means for recouping a loss of something entirely different than the locomotive itself, and to that end has attempted to read into the policy a protection which is not there and for which no premium was paid.

Under these circumstances, we submit that the judgment is not supported by the findings; that it should

be reversed and the lower Court directed to enter judgment in favor of the appellant and cross-appellee, the defendant below.

Dated, San Francisco, California,
July 22, 1935.

Respectfully submitted,

HAROLD M. SAWYER,

L. B. DA PONTE,

ROBERT S. MACFARLANE,

*Attorneys for Appellant
and Cross-Appellee.*

No. 7820

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

NORTH RIVER INSURANCE COM-
PANY (a corporation),
Appellant and Cross-Appellee,

vs.

GUY H. CLARK, as Receiver of the
Montborne Lumber Company (a cor-
poration),
Appellee and Cross-Appellant

BRIEF OF CROSS-APPELLANT AND APPELLEE

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FILED

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GUY H. CLARK, as Receiver of the
Montborne Lumber Company (a cor-
poration),
Appellee and Cross-Appellant

**BRIEF OF CROSS-APPELLANT
AND APPELLEE**

This appeal is taken from a judgment of the District Court of the United States for the Western District of Washington, Northern Division, wherein the court refused to award the cross appellant and appellee a judgment of \$8000.00 on account of damage by fire done to certain logging flat cars owned by the Northern Pacific Railway Company, and in the possession

of the cross-appellant's predecessor in interest at the time of the fire.

For purposes of clarity, the parties will be in this brief referred to as plaintiff and defendant, the positions they occupied in the lower court.

STATEMENT OF FACTS

The plaintiff is the receiver of the Montborne Lumber Company, a Washington corporation, having been appointed as such by order of the state court.

The lumber company conducted a series of logging operations near Montborne, Washington, and in connection therewith, operated a logging railway which connected with the main line of the Northern Pacific at Montborne, Washington. (Tr. p. 33, Par. 3)

On December 19, 1927, a contract was entered into between the Montborne Lumber Company and the Northern Pacific Railway Company (Tr. p. 39, to 41) under the terms of which the lumber company could and would use certain logging flat cars belonging to the railway company for the transportation of the lumber company's logs, and the lumber company agreed

“to pay the Railroad for all damage which cars delivered to it by the Railroad through such connections may sustain from any cause whatever while in its possession.” (Tr. p. 40)

On August 30, 1930, five flat cars belonging to the railway company and in the possession of the lumber company, were derailed and damaged on account thereof in the sum of \$482.13. (Tr. p. 36, Par. 10)

On September 4, 1930, certain other flat cars belonging to the railway company, while in the possession of the lumber company, were destroyed by fire. (Tr. p. 36, Par. 11) The total damage and loss caused by both the derailment and fire was \$8000.00. (Tr. p. 37, Par. 13)

On August 11, 1930, a policy of insurance was issued by the defendant to the Montborne Lumber Company. (Tr. p. 49, Par. 57) This policy insured the Montborne Lumber Company

“against loss or damage caused by fire, derailment or collision * * * to rolling stock as per schedule.” (Tr. p. 50)

In the schedule which is attached to the policy (Tr. p. 57) appears this item:

“12 CARS OWNED by any other than the Assured, consisting principally of Northern Pacific flat cars, main line tanks, and coal gondolas, being an equal amount of coverage on each.” (Tr. p. 57)

There is also attached to the policy a special endorsement, which reads as follows:

“ENDORSEMENT

It is also understood and agreed that this policy

covers the legal liability only of the assured on logging cars owned by others in the possession of the assured, but it is a warranty of this insurance that the insured shall not have at risk an average of more than twelve (12) cars at any one time.

All other terms and conditions remaining unchanged.

This slip is attached to and forms part of Policy No. 11187 of the NORTH RIVER INSURANCE COMPANY issued to MONTBORNE LUMBER COMPANY.

Seattle, Wash. AUGUST 11th, 1930.

(Marine Dept.)

AMERICAN INSURANCE AGENCY

By F. A. FREDERICK, Agent." (Tr. p. 56)

On February 26, 1931, after the appointment and qualification of the receiver of the lumber company, the defendant insurance company paid to the Northern Pacific Railway Company \$8000.00 in full settlement of the railway company's claim against the lumber company on account of the damage to the cars. (Tr. p. 38, Par. 17) This settlement was made without the knowledge or consent of the receiver. Tr. p. 38, Par. 17)

Another phase of this controversy involved the claim on account of the loss of the locomotive which is the subject of an appeal by the defendant and separate briefs have been prepared and filed dealing therewith.

ASSIGNMENT OF ERRORS

The assignment of errors is as follows:

First: The court erred in denying plaintiff's motion made January 14, 1935, for the entry upon the findings of a conclusion of law that the plaintiff is entitled to judgment against the defendant in the sum of \$15,000.00, together with interest from the date thereof, and with plaintiff's costs and disbursements as provided by law, and for entry of judgment for the plaintiff for said sums pursuant to such conclusion, to which denial plaintiff duly excepted and which exception was regularly allowed.

Second: The court erred in construing the insurance policy in this case as not requiring the defendant to pay to the plaintiff \$8000.00, for which the plaintiff was liable to the Northern Pacific Railroad.

Third: The court erred in construing the policy of insurance in this case as an indemnity or liability policy instead of a fire insurance policy.

Fourth: The court erred in holding that the payment by the defendant to the Northern Pacific Railroad Company was an accord and satisfaction of the policy of insurance in this case.

Fifth: The court erred in holding that the parties to the insurance policy intended that the liability of the insured, rather than the loss or damage to the insured was the thing insured against.

Sixth: The court erred in holding that as to plain-

tiff's claimed recovery for damages to the logging flat cars, plaintiff had failed to sustain the burden or proof.

Seventh: The court erred in holding that the plaintiff was not legally liable to the railroad company in the sum of \$8000.00.

Eighth: The court erred in holding the release and discharge of the plaintiff's predecessor in interest, evidenced by "Exhibit 2," to be an accord and satisfaction, and that the plaintiffs wholly failed to prove that as a result of the damage to the cars plaintiff was legally liable to the railroad company in the sum of \$8000.00.

ARGUMENT

The cross appellant's position is this:

The policy sued upon was a policy of fire insurance and under the law of the State of Washington, the only way an insurer may relieve itself of liability on a fire insurance policy is by payment to the named assured.

POLICY WAS A FIRE INSURANCE POLICY

For a determination of this question, we are compelled to look to the policy.

32 C. J. 1095:

"The character of a particular policy is to be

determined by the nature of a contract it expresses, rather than by the nomenclature of the policy, or the character and avowed purposes of the company that issued it.”

Knott vs. Security Mutual Life Insurance Co.
144 S. W. 178

CONTENTS OF POLICY

An examination of the nomenclature of the policy reveals several significant clauses which indicate not only that the policy is not a liability policy, but is a policy insuring against damage caused by certain specific causes.

The first of these portions is the opening paragraph of the policy which reads as follows:

“In consideration of the stipulations herein named and of \$630.00 premium (the company) does insure Montborne Lumber Company from the 8th day of August, 1930, at noon, Standard Time at place of insurance against direct loss or damage as hereinafter provided to an amount not exceeding **TWENTY FIVE THOUSAND TWO HUNDRED DOLLARS**, to Rolling Stock, as per schedule.” (Tr. pp. 49, 50)

A reference to the schedule written on the reverse side of the policy (Tr. p. 57) discloses that only two pieces of equipment are insured, first, the locomotive, and second, the cars involved in this litigation. There is no intimation that the insurance upon the locomotive is a liability insurance.

The rates charged by the insurance company for the

locomotive and the flat cars are the same, to-wit, 21½%.

It is a well recognized and known fact that the rates on liability insurance and fire insurance are not identically the same.

Another section of the policy which clearly indicates that the policy is not one of liability insurance is Section 2 thereof, which reads as follows:

“2. Perils Insured Against.

This Policy Insures Only:

Against loss or damage caused by fire, derailment or collision (coming together of cars and / or locomotives in shifting or coupling not to be considered a collision) collapse of bridges, lightning, cyclone, tornado and flood.” (Tr. p. 50, 51)

PLAINTIFF HAS AN INSURABLE INTEREST

The relationship existing between the lumber company and the railroad company was either one of landlord and tenant, or one of bailor and bailee. That the tenant or bailee, under such a situation, has an insurable interest in the property, is established beyond question.

Delanty vs. Yang Tsze Insurance Assn.
127 Wash. 238

“We are of the opinion, however, that the dredging company did have an insurable interest in the boat by reason of the fact that it had possession of the boat and was at all events liable for the preservation or the value thereof to those whoever had legal right to it. Such possession gave rise to an implied promise on the part of the dredging company to restore the boat to its owner or owners, whoever they might be, though the

lease contract be void for want of power in his surviving partners to execute it * * * * * We conclude that Tacoma Dredging Company had an insurable interest in the boat, and that the policy cannot be avoided for want of such interest in that company."

Counsel may contend that even though the insurance under this policy was in the first instance payable to the Montborne Lumber Company, yet the insurance, having been taken out upon property belonging to the railway company has an equitable lien thereon, entitling it to receive the proceeds of the insurance.

PAYMENT ON FIRE POLICY CAN ONLY BE TO NAMED ASSURED

The above, however, is not the law, in the absence at lease of any covenant in the lease requiring the lessee to take out such insurance, and there was in the contract at bar no such covenant.

A quiet elaborate note on this question is found in **66 A. L. R. 864**, and the general rule is there stated to be as follows:

"It is quite generally held that, in the absence of an agreement to insure between the lessor and lessee, the proceeds of an insurance policy taken out by one of them or his privy cannot be claimed, in whole or in part, by the other, even though the policy covers the value of the interests of both in the property."

To the same effect is **Northern Trust Co. vs. Snyder**, (1896), **22 C. C. A. 47**, **46 U. S. App. 179**, **76 Fed. 34**:

“A landlord may not recover from trustees to whom the lessees conveyed the estate the proceeds of an insurance policy on machinery and fixtures taken out by the lessees and made payable to the trustees, where there was no agreement obligating the lessees to effect insurance on the property for the benefit of the lessor.”

And again, in **Lincoln Trust Co. vs. Nathan (1903)**
155 Mo. 32, 74 S. W. 1007, it is held:

“Where lessees insured themselves against loss in having to pay rent after the building was destroyed, and paid the premiums without any agreement with the lessors, the latter had no right to any of the proceeds of the policy.”

To the same effect, also, is **Batts vs. Sullivan (1921)**
182 N. C. 129, 108 S. E. 511:

“A lessor cannot recover from his lessee one third of the proceeds of a policy of insurance taken out by the lessee at his own expense, without the knowledge of the lessor, to protect the lessee’s interest in tobacco stored in the lessor’s barn, of which the latter was entitled to one-third.”

26 C. J. 436:

“In the absence of any contract between Landlord and tenant as to insurance by one for the benefit of the other, neither has any interest in insurance taken by the other in his own interest. But where the tenant stipulates to keep the premises insured for the benefit of the landlord, the latter is entitled to the proceeds of insurance taken by the tenant, and where the landlord takes out insurance as agent for the tenant, it belongs to the tenant.”

8 Couch on Insurance, Sec. 1935, p. 6438:

“As between the lessor and lessee of property which the lessee has insured against fire, the lessor has no claim to insurance money collected by the lessee, he having been under no obligation to insure for the benefit of the lessor and having paid for the insurance with his own money.

The reason generally ascribed for the rule that a lessor or lessee, or his privy, cannot claim the benefit of insurance taken out by the other or his privy, unless there is an agreement in the lease to insure, is that the contract of insurance is a personal contract of indemnity which does not enure to the benefit of the other party.”

FEATURES OF LIABILITY POLICY

It is true that the endorsement on the policy recites that the policy covers the **legal liability only** of the assured on the logging cars.

This is the only place in the policy where anything sounding in the nature of a policy of liability insurance appears.

While there might be some doubt, under ordinary circumstances, as to whether or not this would create a contract of liability insurance, yet it is to be remembered that this is a contract of insurance and as such is to be strictly construed against the insurance company and in favor of the assured. The Court's attention is respectfully called to the fact that the benefits of this rule of strict construction do not extend to what might be called third party beneficiaries or, as in this

case, the railroad company, but the policy is to be construed strictly against the insurance company and liberally in favor of the assured.

32 C. J. 1152:

“It is a cardinal principle of insurance law that a policy or contract of insurance is to be construed liberally in favor of insured and strictly as against the company. Stated more fully, the rule is that, where, by reason of ambiguity in the language employed in a policy or contract of insurance, there is doubt or uncertainty as to its meaning and it is fairly susceptible of two interpretations, one favorable to insured and the other favorable to the company, the former will be adopted.”

**Thompson vs. American Brotherhood of Yeomen,
130 Wash. 179:**

“Contracts of this character which are indefinite as to their meaning, or subject to two constructions, will ordinarily be construed most strongly in favor of the assured and against the assurer. *Remington vs. Fidelity Deposit Co.*, 27 Wash. 429, 67 Pac. 989; *Algoe vs. Pacific Mutual Life Ins. Co.*, 91 Wash. 324, 157 Pac. 993; *Mountain Timber Co. vs. Lumber Ins. Co.*, 99 Wash. 243, 169 Pac. 591.”

To the same effect are *Green vs. National Casualty Company*, 87 Wash. 237, and *Menger vs. Inland Empire Insurance Co.*, 118 Wash. 514.

Another reason why this policy can not be construed as a liability policy is because it contains none of the covenants usually and customarily contained in a liability policy.

Liability policies are of two kinds, either an indemnity contract or policy, or a liability contract or policy, and the distinction between these two classes of contract is well recognized.

36 C. J. 1057:

“A policy of liability insurance, like ordinary contracts of indemnity, generally, is either a contract of insurance against loss or damage, and is called an ‘indemnity contract’ or an ‘indemnity policy,’ or it is a contract of insurance against liability for loss or damage, and is called a ‘liability contract’ or a ‘liability policy.’ Whether it is the one or the other depends upon the intention of the parties as evidenced by the phraseology of the agreement or covenant in the policy, and the determination of this intention is important in determining the accrual of the insurer’s liability under the policy, there being a marked difference between a contract of insurance against loss and one against liability. If the policy contains conditions inconsistent with the theory of indemnity against damages, or otherwise clearly shows an intention to insure against liability for damages, it will be so construed, and is not merely a contract of indemnity against loss or damage by reason of liability. But where the policy plainly shows an intention only to pay the loss or damages for which insured was liable and has been compelled to pay, it is a contract of indemnity against loss or damage by reason of liability * * * Where the policy provides that insured shall immediately notify the company in case of accident or injury, that the company would defend actions growing out of injuries, in the name of insured, and that insured should not settle any claim or incur any expense without the consent of the company, it is generally held to be a policy of indemnity against liability for damages, and is not merely

a contract of indemnity against damages. On the other hand, it has been held that a provision in the policy, that no action shall lie against insurer as respects any loss unless it is brought by insured himself to reimburse him for loss actually sustained and paid by him in satisfaction of a judgment, is a controlling factor in determining that the policy is one against loss or damage, and not against liability, although there are decisions to the effect that such a provision does not make the contract one of indemnity against damage where other provisions indicate indemnity against liability, particularly where the "no action" clause applies only in case the company denies liability and refuses to defend."

In this connection, the court's attention is respectfully called to the fact that there is no covenant in this contract regarding settlement by the assured, or anyone else, there is no covenant regarding indemnity, and there is no covenant regarding the defense of any asserted liability by a claimant against the assured.

A statement of the usual contents of liability policies is found in **36 C. J. 1110**:

"Liability insurance policies, at the present time, whether liability policies or strict indemnity policies, usually contain provisions to the effect that where suit is brought against insured for an injury covered by the policy, insurer, at its election may: (1) Defend the suit in the name and on behalf of insured, without any further assent or ratification from him, and without any interference by insured in the proceedings. (2) Settle the claim at its own cost. (3) Pay insured the stipulated amount of indemnity, leaving him to defend

himself against the claim as best he may.”

There is in the policy before us neither covenant on behalf of the assured to defend the suit, settle the claim or covenant casting the burden of the defense upon the assured.

Another statement of the rule is found in **36 C. J. 1113:**

“Under most, if not all, liability insurance policies, insurer reserves the right, at its election, to settle any claim against insured for loss or injury covered by the policy.”

In the interpretation of the contract, effect, however, is to be given to all of the language contained therein, and it is respectfully submitted that the most liberal construction which can be given the language of the endorsement would regard it as a limitation of the extent of the liability of the company to the insured.

It is to be remembered that the contract between the lumber company and the railroad company was not made a part of this insurance contract and this limitation upon the amount for which the insurer might be liable was obviously placed in the contract to prevent the lumber company from realizing a profit upon the destruction of cars in its possession and belonging to others.

For example, suppose that the contract between the lumber company and the railroad company provided that in the event of the destruction by fire or otherwise of the cars belonging to the railroad company, that the loss should be borne equally. Under those circumstances, the endorsement on the policy would limit the liability of the insurance company to 50 per cent of the value of the destroyed property and would not permit the lumber company to collect the full value of the property from the insurance company when, in fact, the lumber company would be bound only to reimburse the railroad for 50 per cent of the loss.

Strength is given this contention by the use of the word "only" in the endorsement, for the endorsement reads that the policy covers the legal liability only of the lumber company in respect to these cars.

**ONLY WAY LIABILITY ON FIRE POLICY
DISCHARGED IS BY PAYMENT TO
NAMED ASSURED**

In the final analysis, the loss sustained under this policy was a loss by fire, even though the policy insured against other losses, tornado, cyclone, etc., and there is only one way in which a fire insurer may relieve itself of liability for a loss by fire, and that is by payment to the named assured and to no one else.

26 C. J. 434:

“As the policy is a personal contract between

the insurer and the insured, and not a contract which in any sense runs with the property, the insurance money is generally payable to the person whose interest is covered by the policy, without regard to the nature and extent of his interest in the property, provided he had an insurable interest at the time of making the contract and also at the time of the loss; unless there is a stipulation to the contrary in the policy or unless he has assigned his right to the proceeds, or has by some misrepresentation or change of title or interest defeated his right to recover on the policy."

Another case which very definitely establishes this rule is the case of **Nelson vs. Nelson Neal Lumber Company**, 171 Wash. 55.

The facts in this case were that the Montborne Lumber Company was purchasing on real estate contract a sawmill and other property from the Nelson Neal Lumber Company, the contract of purchase requiring the Montborne Lumber Company to keep the property insured for the benefit of both the vendor and purchaser. Mr. Thomas Smith and Mr. James G. Smith, his son, were officers and trustees of both the Nelson Neal Lumber Company and the Montborne Lumber Company.

The insurance was taken out but the policy was payable to the Montborne Lumber Company only. A fire occurred, the mill was destroyed thereby, and the insurance company paid to the Montborne Lumber Company the face of the policy, \$30,000.00.

The Montborne Lumber Company applied this \$30,000.00, acting through its officers, Mr. Thomas Smith and Mr. James G. Smith, to other debts of the company, paid nothing therefrom to the Nelson Neal Lumber Company, and this suit was instituted by the stockholders of the Nelson Neal Lumber Company against Mr. Smith, his son, and other officers of the two corporations in conversion, and our supreme court held that the insurance money was properly paid to the Montborne Lumber Company, using the following language:

“It is elementary that a fire insurance policy is a purely personal contract, and that payment by the insurer to the insured named in a policy is compulsory. Consequently, payment by the insurer to the Montborne Lumber Company was obligatory in order to acquit the insurer. It necessarily follows that receipt by the Montborne Lumber Company of the insurance proceeds was, in law, necessarily, a corporate act and not an act of the individuals sued herein. *Wilcox vs. Gauntlett*, 200 Mich. 272, 166 N. W. 856. Whatever may have been the liability of that corporation for conversion of the insurance fund, is not here at issue, for it is not sued.”

CONCLUSION

In conclusion, it is respectfully submitted that the policy was a purely personal contract between the assured and the defendant and that payment by the defendant company to the receiver is compulsory, that that liability has not been discharged and that plain-

tiff should recover the amount of the damage sustained.

Respectfully submitted,

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In the
United States Circuit Court
of Appeals
For the Ninth Circuit

No. 7820

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Appellant and Cross-Appellee,

vs.

GUY H. CLARK, as Receiver of the MONTBORNE
LUMBER COMPANY, a corporation,
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BRIEF OF CROSS-APPELLEE

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Appellant and Cross-Appellee,

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GUY H. CLARK, as Receiver of the MONTBORNE
LUMBER COMPANY, a corporation,
Appellee and Cross-Appellant.

BRIEF OF CROSS-APPELLEE

As has been done in the brief of appellant and in the brief of cross-appellant, in this brief we shall continue to refer to the parties as plaintiff and defendant, the positions they occupied in the lower court.

STATEMENT OF FACTS

All of the facts involved in this cross appeal are contained in stipulations which are complete and concise. (Tr. 33-57). For the convenience of the court, however, we wish to summarize the salient features of this controversy.

This action was instituted by the receiver of the Montborne Lumber Company on May 2, 1931, against the defendant to recover losses under a policy of insurance.

The policy in question (Tr. 49-57) specifically insured a certain Shay logging locomotive belonging to plaintiff and also covered

“ . . . the legal liability only of the assured on logging cars owned by others in the possession of assured . . . ”

against certain hazards including derailment, fire, collision, collapse of bridges, lightning, cyclone, tornado and flood.

A forest fire occurred on September 4, 1930, destroying certain bridges and trestles on the logging railroad, so that the Shay locomotive was marooned in the woods. The locomotive itself was never in contact with the fire and sustained no physical damage. The trial court allowed recovery for the stipulated value of the locomotive. This recovery is the basis of de-

fendant's appeal, upon which question a brief has heretofore been served and filed. The cross appeal concerns itself only with the denial of recovery on account of damage to certain Northern Pacific logging flat cars.

The complaint sets out three causes of action as follows:

First Cause of Action

In the first cause of action, in addition to the Shay locomotive, the receiver seeks to recover for the loss occasioned by the destruction of 12 Northern Pacific logging flat cars by the forest fire which occurred September 4, 1930.

Second Cause of Action

The second cause of action involves 5 additional Northern Pacific logging flat cars. Recovery is sought under the insurance policy for derailment alleged to have occurred August 30, 1930.

Third Cause of Action

The third cause of action seeks recovery for 5 additional Northern Pacific logging flat cars. It is alleged that these cars were derailed on August 30, 1930, and while so derailed were, on September 4, 1930, destroyed by fire. Recovery is sought for this loss.

The following facts bearing upon the questions of law presented in the cross appeal are shown by the stipulations:—

(a) 22 Northern Pacific logging flat cars were in the possession of plaintiff under an interchange agreement dated December 19, 1927, and attached as Exhibit 1 to the stipulation (Tr. 39). This agreement provided for the use by plaintiff of Northern Pacific logging flat cars. In this connection it is therein provided:

“The Lumber Company agrees to pay the railroad for all damage which cars delivered to it by the railroad . . . may sustain from any cause whatever while in its possession . . . ”

(b) On August 30, 1930, 5 N. P. flat cars were derailed and damaged in the amount of \$482.13, which damage was fully repaired *by the Railway Company at its expense*.

(c) On September 4, 1930, these 5 cars and 17 additional N. P. cars were in possession of the plaintiff and were destroyed by a forest fire.

(d) “ . . . the loss and damage caused by derailment and/or fire to all of said cars was in the total sum of \$8,000.”

(e) The plaintiff became insolvent and went into receivership some time after the fire.

(f) On November 28, 1931, an amended claim in the receivership was filed by the Northern Pacific. This amended claim is attached to the stipulation as Exhibit 3 (Tr. 35). As to the flat cars which form the basis of the first, second and third causes of action, the Northern Pacific in the amended claim states:

"That it neither had nor makes any claim against said Montborne Lumber Company or said receiver, for or on account of any legal liability or otherwise for damage to or failure to return" said cars "... and releases and discharges said Montborne Lumber Company and its receiver from any and all legal liability for or on account of damage to said cars or failure to return the same pursuant to the interchange contract above referred to or otherwise."

(g) On February 26, 1931, the defendant Insurance Company paid to the Northern Pacific the sum of \$8,000 in full settlement and satisfaction of any and all claims the Northern Pacific might have against the defendant Insurance Company or the plaintiff Lumber Company on account of the damage to or destruction or loss of any and all cars of the Northern Pacific covered by the said policy of insurance.

SUMMARY OF ARGUMENT

The defendant's position on this cross appeal is this: The policy in question so far as the Northern Pacific logging flat cars are concerned is either an indemnity or a liability policy. In either event, plaintiff is not entitled to recover because:

(A) If it is an indemnity policy the plaintiff cannot recover, because:

- (1) The claim has been extinguished; or,
- (2) The plaintiff has no claim against the defendant until it has sustained *and* paid the loss.

(B) If it is a liability policy, plaintiff cannot recover, because:

- (1) The claim is extinguished;
- (2) The Northern Pacific could sue the plaintiff direct and enforce collection against defendant. The court will not compel an idle act.

There are two additional defenses to plaintiff's action:

- (1) Plaintiff cannot show an existing liability to the Northern Pacific.
- (2) A constructive trust in favor of the owner of property is impressed upon the proceeds of an insurance policy taken out by a party in possession, even if taken without the knowledge of the owner.

The Issue

Reduced to its lowest terms the question of law for determination is whether or not the defendant is liable to the plaintiff for the destruction of Northern

Pacific flat cars under an insurance policy insuring the plaintiff against the legal liability only of the plaintiff to the Northern Pacific, when the Northern Pacific has received full satisfaction for said destroyed cars and has released the plaintiff from any legal liability.

Stated in another way, may the plaintiff collect from the defendant as and for legal liability to the Northern Pacific when the Northern Pacific makes no claim and releases and discharges the plaintiff from all liability?

ARGUMENT

Plaintiff's Contention

As stated on page 6 of plaintiff's brief as cross-appellant, it is plaintiff's position that

"The policy sued upon was a policy of fire insurance and under the law of the State of Washington, the only way an insurer may relieve itself of liability on a fire insurance policy is by payment to the named assured."

The difficulty with plaintiff's argument is that, in substance, it ignores or rejects the plain language of the policy in question and assumes the fundamental fact necessary to otherwise sustain its position.

Policy is Not a Fire Insurance Policy

So far as the Northern Pacific flat cars are concerned, the policy is not, strictly speaking, a fire insurance policy on certain specific property. By the very language of the endorsement of the policy "*the legal liability only*" as to the flat cars is covered by the policy.

The endorsement on the policy reads (Tr. 56):

"It is also understood and agreed that this policy covers the *legal liability only* of the assured on logging cars owned by others in the possession of the assured . . . " (*Italics ours*).

A brief reference to the situation of the parties and the facts will show that the policy, so far as the logging flat cars are concerned, was never intended to be other than what the language of the endorsement recites.

It will be noted by a reading of the policy that two classes of property are involved, (1) a Shay locomotive owned by plaintiff; (2) logging flat cars owned by others.

The stipulation shows (Tr. 35):

"(7) That on August 11, 1930, and for a long time prior thereto, and until the time of the fire before mentioned, the Railway Company furnished the Lumber Company its flat cars, main line tanks and coal gondolas for the purpose of loading and/or unloading

freight under said interchange agreement; that the Lumber Company did not own any logging flat cars, main line tanks or coal gondolas, and that all rolling equipment of said character used or intended to be used at any time material to this litigation upon the logging railroad of the Lumber Company was rolling equipment owned by the Railway Company and furnished pursuant to the said interchange agreement."

and further shows (Tr. 37):

"(2) That no flat cars, main line tanks or coal gondolas other than those herein described belonging to others than the Lumber Company were upon the logging railroad or in the possession of the Lumber Company at the time of the fire."

It will be noted, therefore, that the only rolling equipment other than the plaintiff's own property (the Shay locomotive), which was intended by the parties to be covered by the insurance policy was rolling equipment of the Northern Pacific. No "main line tanks or coal gondolas" were damaged,—hence this controversy concerns only N. P. logging flat cars in the possession of plaintiff pursuant to the interchange agreement.

Under the interchange agreement of December 19, 1927 between the Northern Pacific and plaintiff (Tr. 39-41):

"The Lumber Company agrees to pay the Railroad for all damage which cars delivered to it by the Railroad . . . sustain from any cause whatever while in its possession . . . "

It is apparent, therefore, that in view of this interchange agreement, the insurance which plaintiff obtained through defendant was for the obvious purpose of protecting it from possible liability in the event of damage to the cars of the Northern Pacific.

The fact that the policy is not limited to damage by fire, is the best evidence that it is not a fire insurance policy. The policy also insured against the hazards of derailment, collision, collapse of bridges, lightning, cyclone, tornado and flood. By the express terms of the endorsement attached to the policy it was not direct insurance of property, so far as these cars were concerned, but only insurance against *legal liability* proximately caused by the named hazards.

Thus, if damage had occurred to one of the Northern Pacific logging flat cars by flood, (a hazard insured against) but for which the plaintiff was not legally liable to the Northern Pacific, plaintiff could not recover from defendant therefor.

That this is not a fire insurance policy is further evidenced by the stipulation (Tr. 36) showing that five of the flat cars were derailed prior to the fire and were repaired by the Railway Company at its own expense. The Railway Company of course had a valid claim for this item under the interchange agreement.

trial court in its memorandum decision reported in 8 F. Supp. 394 (Tr. 62 and appendix to this brief) :

“In the law relating to insurance as well as other contracts, the rule is that specific provisions must control over general provisions, and construing the policy, together with said endorsement, it is obvious that the parties intended that liability of the assured rather than loss or damage to the insured, was the thing insured against.”

As previously stated, plaintiff construed the effect of this policy of insurance just as if the endorsement were not a part of it. But even such a view will not avail plaintiff for, if the endorsement be emasculated or ignored, then, under the stipulation of facts, there can be no recovery to plaintiff because the plaintiff has no interest or partial ownership in the property. The sole basis of any recovery whatever, therefore, is necessarily predicated on plaintiff's liability over to the Northern Pacific. If this be not so, then this becomes a pure wagering contract, and of course is void.

“If the person procuring or holding the contract of insurance has no such interest, the contract is invalid, the objection to such contract being that there is a mere wager on an event in the happening of which insured has no interest.”

26 C. J. 18.

Fire Insurance Policy is an Indemnity Policy

It was the position of plaintiff below, and the plaintiff apparently in its brief adheres to the view, that a

fire insurance policy is neither an indemnity nor liability policy. Plaintiff conceded in the court below, and we gather from its brief on appeal, that if the policy in question is in fact not a fire insurance policy, but either an indemnity or liability policy, the insurer may extinguish the liability or discharge the claim indemnified against without the consent of the assured.

The policy in question is either an indemnity policy or liability policy and, as will be developed hereinafter, whichever view is taken of the policy the result is the same. Plaintiff cannot recover.

All insurance, except life, can be generally classified as either indemnity or liability, depending upon whether the insurance is against loss, or against liability for loss.

Generally speaking, a fire insurance policy, (except as provided by specific endorsement), when it is an insurance for loss by fire to property, is an indemnity policy because it is an insurance against loss.

“The contract of (fire) insurance, as all know is a contract of indemnity upon the terms and conditions specified in the policy of insurance.”

Glendale Woolen Co. v. Protection Ins. Co., 21 Conn. 19, 31.

“The general, if not universal, rule is that fire insurance contracts are purely indemnity contracts * * *”

Millard v. Beaumont, 185 S. W. 547, (Mo.).

A fire insurance policy is—

“A contract of indemnity * * * to reimburse the insured for an actual loss (by fire) not exceeding an agreed sum.”

Getchell v. Mercantile, etc., F. Ins. Co., 83 Atl. 801 (Me.).

“A fire policy is a contract to indemnify in case of loss.”

Commonwealth v. American Life Ins. Co., 29 Atl. 660 (Pa.).

“Fire insurance is a contract of insurance by which the insurer for a consideration agrees to indemnify the insured against loss of or damage to property by fire. * * * The contract is of indemnity only. * * *”

26 C. J. 17.

We, therefore, respectfully submit that *under all authority*, strictly speaking, a fire insurance policy is an indemnity policy, except where the policy is removed from this classification because of specific endorsement.

Distinction Between Indemnity and Liability Policy

The distinction between the two classes of insurance policies has been thus stated by the Supreme Court of the State of Washington:

“The test as to whether this is a liability or indemnity bond seems to be: If the intention of the parties thereto was to protect the assured from liability for damages, or to protect persons damaged by injuries occasioned by the assured, as specified in the contract, when such liability should accrue and be imposed by law (as by a judgment of a competent court), it is a liability bond; if, on the other hand, it is only to indemnify the assured against actual loss by them—that is, for reimbursement to them for moneys they had been obliged to pay and had paid, it would be an indemnity bond only, protecting only the assured.”

Fenton v. Poston, 114 Wash. 217, 224; 195 Pac. 31.

To the same effect see *Ford v. Aetna Life Ins. Co.*, 70 Wash. 29, 126 Pac. 69, and cases therein cited. Judge Gose, in commenting upon one of the cited cases, says:

“The policy was identical in meaning with the policy in controversy. The court said, that the policy insured against loss only; that no obligation arose until the assured had paid the loss;”

Ford v. Aetna Life Ins. Co., 70 Wash. 29, 35, 126 Pac. 69.

Assuming Indemnity Policy

If, then, the policy we are considering is construed to be an indemnity policy, the assured cannot maintain its cause of action until it has actually suffered and paid the loss. The basis of recovery under an indemnity policy is not threat of loss, but actual loss.

Ordinarily, as above pointed out, a fire insurance policy is construed to be an indemnity policy, and the rights under an indemnity policy are usually personal to the assured, but this generalization is of no avail to plaintiffs because this is not a fire insurance policy in the ordinary sense of the expression. It is an insurance against *legal liability only*. Construed, however, as an indemnity policy, under the facts disclosed in the stipulation there has been no actual loss and there can be no actual loss and there will be no actual loss to the plaintiff until the plaintiff first pays to the Northern Pacific the value of the destroyed flat cars.

We also particularly draw the attention of the court to the rule that even in an indemnity policy where the assured must first sustain and pay the loss before any right under the policy accrues, the Insurance Company may of its own volition deal with and extinguish the claim of the injured or damaged party against the assured.

Thus in *Sanders v. Frankfort Marine, etc., Ins. Co.*, 57 Atl. 655 (N. H.), in which case the policy was assumed to be an indemnity policy, the Supreme Court of New Hampshire said:

“But whether such power exists or not, the indemnitor has the right to perform his contract of indemnity by payment of the claim indemnified against.” (p. 656.)

There is no question as to this rule. We have found *no* cases to the contrary, and plaintiff has not contended otherwise. At all events it is logical that the rule should be as stated. When a person is damaged and makes claim against an insurer because thereof, there can be no substantial reason for denying the right of the insurance company under an indemnity policy to extinguish this claim by settling direct with party damaged. While it is true, under the weight of authority, that the injured party would not have a cause of action direct against an insurance company on an indemnity policy, still if the insurance company elects voluntarily to extinguish the claim, there can be no cause of complaint.

The assured cannot complain because—

(1) The claim has been extinguished.

(2) The assured would have no claim against the Insurance Company until first it had sustained and paid the loss.

In considering the cases involving policies of insurance, courts frequently have been careless in distinguishing between indemnity and liability policies. In those cases, however, wherein the specific question is tendered as to the distinction between the two classes of policies, there is no confusion. We draw this particularly to the attention of this court because in some

cases wherein the distinction has not been presented and was not necessarily to a decision, language is used which is obviously without reference to the particular character of the policy in question.

So much for a consideration of the policy in question construed as an indemnity policy. Clearly plaintiff is not aided by such a view.

“No obligation arose until the assured had paid the loss.”

(*Ford v. Aetna Life Ins. Co., supra.*)

Moreover, the claim has been extinguished because—

“* * * the indemnitor has the right to perform his contract of indemnity by payment of the claim indemnified against.”

(*Sanders v. Frankfort Marine, etc., Ins. Co., supra.*)

This the indemnitor has done in the instant case. It has paid the claim indemnified against by paying the Northern Pacific Railway Company.

In this connection, assuming the policy in question to be a fire insurance policy, we wish to call attention to the case particularly relied on by plaintiff, *Nelson v. Nelson Neal Lumber Co.*, 171 Wash. 55, 17 Pac. (2d) 626. In addition to this case many others might be cited to the proposition that payment by the insurance company to the named assured would discharge

the liability of the insurance company. That is all that the *Nelson* case holds. It is but common sense to hold that payment by the insurance company to the named assured, without knowledge or notice of the rights of third parties, has the effect of discharging the liability of the insurance company. But the *Nelson* case and similar cases which might be cited are not authority on the question as to whether or not extinguishment of the liability or claim indemnified against does not also discharge the insurer. There is no inconsistency between the two propositions.

Assuming Liability Policy

On the other hand, assuming that the policy is of the character which is generally described as a liability policy, plaintiff is not aided.

In the first place, in a liability policy, as in an indemnity policy, the insurance company may settle direct with the party injured or damaged. Thus, in *Anoka Lumber Co. v. Fidelity & Casualty Co.*, 65 N. W. 353, (Minn.), which involved a liability policy, the court held that the insurance company had the right to assume and settle or pay the claim of the injured party.

We have found *no* cases to the contrary and plaintiff has not contended otherwise. In logic this must

be so. The assured is not damaged because the claim is extinguished; the party injured cannot complain because his claim is satisfied. There is a full performance by the insurance company by the assumption and payment of the liability.

Secondly, under the decisions, if the Northern Pacific sued and obtained judgment against the plaintiff for the destruction of the cars, (which, of course, it would have a right to do), it could immediately proceed against the Insurance Company direct and enforce collection without the proceeds of the policy passing through the hands of the assured. That this is so has been held in the case of *Fenton v. Poston*, 114 Wash. 217, 195 Pac. 31, involving a liability policy, and where a garnishment after judgment was successfully invoked.

This court will not compel an idle act as a condition precedent to the legal approval of that which has already been accomplished, and which would be accomplished by the performance of the ritualistic act.

Apart from the foregoing considerations, there are two further insurmountable defenses to plaintiff's action:

No Existing Liability

(1) Assuming a destruction of the flat cars by fire, unless the plaintiff is legally liable by reason thereof

to the Northern Pacific, it could not successfully maintain its action against the Insurance Company. Stated in another way, it is essential to plaintiff's cause of action that it plead and prove an existing legal liability to the Northern Pacific. Here the Northern Pacific has released its claim against the plaintiff. It would be an anomalous situation to permit a recovery as and for a liability which has been extinguished and is non-existent.

Rule of Constructive Trusts

(2) A constructive trust in favor of the owner of property is impressed upon the proceeds of an insurance policy taken out by a party in possession, even if taken out without the knowledge of the owner.

There is no question but that the delivery of possession of personalty for the purpose of transportation and for use and return is a bailment.

6 C. J. 1099

"A bailment may be defined as a delivery personalty for some particular purpose * * upon a contract, express or implied, but after the use has been fulfilled, it shall be redelivered to the person who delivered it * * *"

6 C. J. 1084.

Here, the plaintiff was a bailee in possession of flat cars owned by the Northern Pacific. An insurance policy was taken out by the bailee. Even if it be as-

sumed that the insurance policy was taken out without the knowledge of the owner, in the event of the destruction of the property the proceeds of the policy are impressed with a trust in favor of the owner.

“And one having an interest in the property, may claim the advantage of the policy, although it was taken without his direction or knowledge, a ratification or adoption of the act of the holder of the property insuring it for the benefit of others being sufficient;”

26 C. J. 444.

To the same effect, in addition to cases hereinafter cited, see:

Waters v. Monarch Life & Fire Ins. Co., 25 L. J. Q. B. 102 (1856);

Waring v. Indemnity Fire Ins. Co., 45 N. Y. 606;

Stillwell v. Staples, 19 N. Y. 401.

It is axiomatic that one may not maintain an action on a policy of insurance which he has obtained unless he has an insurable interest therein.

“If the person procuring or holding the contract of insurance has no such interest, the contract is invalid, the objection to such contract being that there is a mere wager on an event in the happening of which insured has no interest.”

26 C. J. 18.

Here the plaintiff as bailee of these flat cars, had as its only insurable interest its contractual liability to the Northern Pacific in the event of damage, loss or

destruction of the cars. Stated in another way, the only conceivable loss which the plaintiff could sustain as to the flat cars, would be its liability to the Northern Pacific Railway Company. Its liability to the Northern Pacific was all inclusive, because the plaintiff agreed to pay the railroad for all damage to the cars "from any cause whatsoever while in its possession". To make this a valid contract of insurance, therefore, requires that it be construed so as to give the plaintiff an insurable interest. This does not mean, however that the property cannot be insured for its full value by the plaintiff:

"Any bailee or person in custody of property and responsible for it may take insurance in his own name, and may recover not only a sum equal to his own interest in the property, * * * but the full amount in the policy up to the value of the property."

26 C. J. 25.

When, therefore, insurance is taken out by a bailee or one holding property in trust, even without the knowledge of the owner, the interest of the true owner is protected and the proceeds of the policy in the event of loss is a trust fund for the benefit of the owner:

"The insurance is not, however, merely on the interest of the one who takes out the policy, but covers the entire value of the property; and insured may recover such value, accounting to the real owner, who sees fit to avail himself of the benefit of the insurance, for any excess beyond the interest or liability of insured, although the insurance may be so taken as to

cover only the liability of the insured and preclude any recovery by him for the benefit of the owner. The owner of the goods may adopt the benefit of the policy even after a loss. As a rule, no act or omission of the person procuring the insurance can defeat the recovery by the owner of the goods of his share of the proceeds."

26 C. J. 86.

Home Insurance Co. v. Baltimore Warehouse Co.

The leading case in this country in support of the principles above stated and in support of the rule that if the plaintiff successfully maintained its action here against the Insurance Company the proceeds would be impressed with a trust in favor of the Northern Pacific, is the case of *Home Insurance Company of New York v. Baltimore Warehouse Co.*, 93 U. S. 527, 23 L. Ed. 868.

In this case the insurance company issued to the warehouse company a policy of fire insurance "on merchandise; their own, or held by them in trust, or in which they have an interest *or liability*". At the time of the loss, the property was in the possession of the warehouse company as bailee. The owners of the property also took out insurance upon the same property. The question was as to contribution between the policies. The court below charged the jury that these policies, if upon the same property, were liable to contribution. The insurance company con-

tended that only the interest of the warehouse company in the goods was insured. Concerning the meaning of the policy, the court said:

“In those cases, as in all others, the subject of the insurance, its nature and its extent, are to be ascertained from the words of the contract which the parties have made. It is true of policies of insurance as it is of other contracts that, except when the language is ambiguous, the intention of the parties is to be gathered from the policies alone. There are cases in which resort may be had to parol evidence to ascertain the subject insured; but they are cases of latent ambiguity. So, in the construction of other contracts, parol evidence is admissible to explain such ambiguities. In this particular, the rule for the construction of all written contracts is the same. Lord Mansfield said long ago that courts are always reluctant to go out of a policy for evidence respecting its meaning. *Lorraine v. Thomlinson*, Doug., 585. And so are the authorities generally. *Astor v. Ins. Co.*, 7 Cow. 202; *Murray v. Hatch*, 6 Mass. 465; *Levy v. Merrill*, 4 Me. 180; *Ins. Co. v. Loney*, 20 Md. 36; *Arn. Ins.*, 1316, 1317, and n.; 2 Greenl. Ev. 377.”

* * * *

“Turning, then, to the policy issued to the plaintiff below, and construing it by the language used, the intention of the parties is plainly exhibited. Its words are: The Home Insurance Company ‘insure Baltimore Warehouse Company against loss or damage by fire, to the amount of \$20,000, on merchandise hazardous or extra hazardous, their own or held by them in trust, or in which they have an interest or liability, contained in’ a certain described warehouse. There is nothing ambiguous in the description of the subject insured. It is as broad as possible. The subject was merchandise stored or contained in a warehouse. It was not merely an interest in that merchandise. The

merchandise of the Warehouse Company, owned by them, was covered, if any they had. So was any merchandise in the warehouse in which they had an interest *or liability*. And so was any merchandise which they held in trust. The description of the subject must be entirely changed before it can be held to mean what the insurers now contend it means." (p. 869.)

* * * *

"It is, undoubtedly, the law that wharfingers, warehousemen, and commission merchants, having goods in their possession, may insure them in their own names, and in case of loss may recover the full amount of insurance, for the satisfaction of their claims first, *and hold the residue for the owners*. Waters v. Assur. Co., 5 Ell. & Bl. 870; R. Co. v. Glyn, 1 Ell. & Ell. (Q. B.) 652; DeForest v. Ins. Co., 1 Hall 136; Siter v. Morris., 13 Pa. St. 219." (p. 869.) (Italics supplied).

The court points out that the warehouse receipts contained notices that the warehouse company held the property as bailees only, "and was not insured by the corporation." The court then concludes:

"Without pursuing this discussion further, we have said enough to vindicate our opinion that the policy upon which this suit was brought covered the merchandise held by the Warehouse Company on storage, and not merely the interest of the bailee in that property. It follows, necessarily, that there was double insurance. The policy issued to the Warehouse Company and those obtained by the depositors of the merchandise, covered the same property, and they were for the benefit of the same owners. The persons assured were the same; for if the policies taken out by Hough, Glendennin & Co. were upon their goods, notwithstanding the memorandum that the loss, if any, was payable to the Baltimore Warehouse Company,

as may be conceded was the case, so was the policy now in suit. The insurers are liable, therefore, *pro rata*, each contributing proportionately." (p. 870.)

To the same effect:

"It was lawful for the plaintiff to insure in its own name goods held in trust by it; and it can recover for the entire value, holding the excess over its own interest in them for the benefit of those who have entrusted the goods to it." (Citing cases.)

California Insurance Co. v. Union Compress Co.,
133 U. S. 387, 10 S. Ct. 365.

"But a carrier has such an insurable interest in goods entrusted to it for carriage, that it may insure, not only its interest or its liability, but the whole value of the goods, and in such case it may collect the whole value, and, after reimbursing itself for its special loss, *it will hold the surplus in trust for the owner.* 1 Wood, Ins. Sec. 294; *Home Ins. Co. v. Baltimore Warehouse Co.*, 93 U. S. 541. An insurance for the benefit of a carrier upon the goods in its custody, not limited to an insurance of its liability or interest, is an insurance of the whole value, and one in which the owner has an interest. The case of *Home Insurance Co. v. Baltimore Warehouse Co.* is an instructive and well-reasoned case, and meets our approval."

Lancaster Mills v. Merchants' Cotton-Press & S. Co.,
14 S. W. 317 (Tenn.), per Judge Lurton.

See also, *Fire Insurance Assn. v. Merchants & Minors Transportation Company*, 7 Atl. 905, (Md.); *Brooklyn Clothing Corporation v. Fidelity Phoenix Fire Ins. Co.*, 200 N. Y. S. 208.

It will be noted that this principle of law is ancient. In the *Home Insurance Company* case, *supra*, the

ance, Sec. 1935, p. 6438, and a note to be found in 66 A. L. A. 864, all to the effect that a lessor may not recover on an insurance policy taken out by the lessee unless there be a covenant in the lease requiring the lessee to take out such insurance.

It will be noted that the foregoing cases and citations deal with the relationship of lessor and lessee. The same rule is similarly stated as to landlord and tenant (26 C. J. 436), vendor and purchaser (26 C. J. 437), and mortgagor and mortgagee (26 C. J. 438), although there is respectable authority *contra*.

Passing any question as to the general rule cited by plaintiff, there is a specific exception as well recognized as the rule itself. The exception applicable to bailments is stated at 26 C. J. 443-444. As already shown in the case of *Home Insurance Co. v. Baltimore Warehouse Co.*, *supra*, the Supreme Court of the United States itself has recognized the exception to the general rule.

Robert Williams & Co. v. Auto Express Co.

A case squarely in point, recognizing the exception to which we have just referred, and which is not to be distinguished from the instant matter, is *Robert Williams & Co. v. Auto Express Co.*, 78 Atl. 670, (N. J. Equity).

Plaintiff delivered silk ribbons to defendant for transportation to New York. It was destroyed by fire while in possession of the carrier. The carrier "had previously procured insurance against loss or damage by fire on merchandise consisting principally of silk and silk goods in transit * * * and for which they are *liable* as common carriers." The carrier made an assignment to the shipper just before the carrier's insolvency. Both the shipper and the receiver for the carrier claimed the money.

Relying on the cases of

Home Ins. Co. v. Baltimore Warehouse Co., 93 U. S. 527, 23 L. Ed. 868;

California Ins. Co. v. Union Compress Co., 133 U. S. 387, 33 L. Ed. 730;

Waters v. Monarch Ins. Co., 5 El. & Bl. 870, 25 L. J. Q. B. 102;

Stillwell v. Staples, 19 N. Y. 401;

Waring v. Indemnity Fire Ins. Co., 45 N. Y. 606, 6 Am. Rep. 146;

Lancaster Mills v. Merchants' Cotton Press Co., 14 S. W. 317, 24 Am. St. Rep. 586, (Tenn.);

Fire Ins. Assn. v. Merchants' Co., 7 Atl. 905, 59 Am. Rep. 162, (Maryland);

Roberts v. Firemen's Ins. Co., 30 Atl. 450, 44 Am. St. Rep. 642 (Pennsylvania)

the court holds:

"The phraseology of the insurance policy in this case is not substantially different from that contained in

the policies adjudicated upon in the cases above cited. In each and all of the cases the policy was procured by a bailee, and was for the benefit of a bailor, and in every case was held to be direct insurance on the goods of the bailor, thus giving the bailor an interest in the policy from the time of its issuance. This interest is, however, subject to any interest which the bailee may have under the policies. It appears in this case that the bailee has no interest to protect, and that therefore whatever moneys are derived from the policies belong to the bailor.

“It was argued that the assignment made by the express company to the petitioner of an interest in this fund was invalid for the reason that the assignment was made of assets of the corporation in contemplation of insolvency, and that there was thus a violation of the terms of section 64 of our corporation act, P. L. 1896, p. 298. If the petitioner’s right stood on the assignment there might be some reason for this contention, but it does not so stand. Whatever right the petitioner has arose out of the policies of insurance, and became efficient for the petitioner’s protection as soon as the insurance was effected.” (p. 672.)

This case, therefore, if viewed from the standpoint of a liability policy, must be resolved in favor of the Insurance Company by the application of the fundamental principle enunciated by the foregoing cases and citations, that:

The Insurance Company having paid the Railway Company, plaintiff cannot maintain this action because the proceeds of an insurance policy taken out by a bailee is impressed with a constructive trust in favor of the bailor (Railway Company) even if the

policy is taken out without the knowledge of the bailor.

This case is therefore to be resolved exactly as if the Northern Pacific, the owner of the cars, had been named beneficiary in the endorsement. In such a case, of course, plaintiff would not even contend that the Insurance Company did not properly apply the fund. This must be so because the endorsement insures against "legal liability". The legal liability is that of the insured to the Northern Pacific.

It follows, therefore, that whether the insurance policy be construed as an indemnity policy or a liability policy, the result is the same—plaintiff cannot successfully maintain its action.

We again desire to recur to the basic facts, which, in and of themselves, are decisive and controlling:

(1) The insurance policy is against *legal liability only*.

(2) There is no legal liability.

What is "legal liability"? In *Royal Insurance Co. v. St. Louis, San Francisco Ry. Co.*, 291 Fed. 358, the policy insured a railroad against legal liability for cotton carried by it and destroyed by fire. The court held legal liability was established by a judgment in the State Court holding the carrier liable in an action

by the shipper, of which action the insurer could assume the defense. As to the definition of what constitutes legal liability, the court said:

“As we understand it, the term ‘legal liability’ in such contracts as is involved in this action, is a liability which our courts of justice, in this country, recognize and enforce as between parties litigant therein.”

To the same effect see 5 Couch on Insurance, Sec. 1210.

Under the facts shown by the stipulation, is there a liability which the Northern Pacific can *enforce* against the plaintiff? There are many answers,—one is sufficient. The Northern Pacific has released the plaintiff.

Liability must be such as to be *enforceable* in a court of justice. Can the Northern Pacific enforce liability against the plaintiff in the face of a release *and* full recoupment for its loss?

The purpose of the policy in question was to protect the insured from having to pay the Northern Pacific for loss of its cars. The insured was not seeking to protect itself against loss of its own property because it did not own the cars. If the insured be protected from having to pay the owner of the cars for their loss, the policy has served every purpose for which it was procured. This is exactly what has hap-

pened, for payment by the defendant to the Northern Pacific has extinguished the liability of the insured to the railway company and it has received full release from the railway company. Therefore, as the policy has fully accomplished the purpose for which it was taken out, the insured has received full value for the premium paid.

Plaintiff brings this action not to protect the Northern Pacific, but with the hope that the proceeds of the insurance belong to the receiver for distribution to preferred and general creditors, divested of any trust character.

Had insured remained solvent, certainly it would not have brought the case at bar for it could not possibly make a profit therefrom. The fortuitous circumstance that insured went into the hands of a receiver certainly did not increase the rights it otherwise had. The only change in the situation arising out of the insolvency of insured is the desire, doubtless commendable, of the receiver to secure money to divide among other creditors. But creditors have sustained no loss of which they can complain. They had no interest in the cars. Only the Northern Pacific sustained a loss and only it should receive reimbursement from the fund created by insured for the very purpose of indemnifying that loss.

In good conscience, we ask: *Who suffered this loss?* The plaintiff has suffered no loss by destruction of these 22 cars, only 12 of which are covered by the policy.

The Northern Pacific is the only one sustaining a loss by reason of their destruction. The plaintiff cannot recover until it has suffered a loss. It never will suffer a loss because the claim of the Northern Pacific is released and extinguished. Nor is there an existing and enforceable legal liability.

Finally,—suppose the Northern Pacific were now suing the plaintiff for the non-return of the flat cars. Would it not be a good defense for the plaintiff to show its release and discharge? *The Insurance Company is entitled to raise any defense in this action that the plaintiff could raise against the Northern Pacific.* Without a right in the Northern Pacific to enforce a claim against the plaintiff, the plaintiff has no right against the Insurance Company. Water cannot rise higher than its source.

The defendant is entitled to an affirmance of the judgment insofar as it denies recovery on account of the N. P. logging flat cars.

SUMMARY

Summarizing our position:

If the policy be viewed as an indemnity policy, then—

(a) Plaintiff has not yet suffered actual loss, and until it does suffer actual loss it has no cause of action. (*Ford v. Aetna Life Ins. Co.*, 70 Wash. 29, 126 Pac. 69);

(b) An indemnitor has the right to extinguish the claim indemnified against. (*Sanders v. Frankfort Marine, etc., Ins. Co.*, 57 Atl. 655, N. H.)

If the policy be viewed as a liability policy, then—

(a) Legal liability has been extinguished by the waiver and releases executed by the Northern Pacific to the plaintiff and to the Insurance Company.

(b) The Northern Pacific could not enforce a liability against the plaintiff for which it has been fully compensated;

(c) If the Northern Pacific is entitled to judgment against the plaintiff, then the Northern Pacific would be entitled to immediately proceed directly against the Insurance Company by garnishment or otherwise. (*Fenton v. Poston*, 114 Wash. 217, 192 Pac. 31.) This being so, and the stipulation showing that the Insurance Company has already paid the Northern

Pacific, there can be no basis of complaint on the part of the plaintiff. In other words, to recover plaintiff must prove that the Northern Pacific has a cause of action against it. When plaintiff has proved this, then it follows as a matter of law that the Northern Pacific is entitled in turn to judgment direct against the Insurance Company by garnishment or otherwise;

(d) An insurer under a liability policy may also settle direct with the party damaged (*Anoka Lumber Co. v. Fidelity & Casualty Co.*, 65 N. W. 353, Minn.) This is all that has taken place in the case at bar.

In addition to the foregoing reason, we say that whether the policy be an indemnity or liability policy:

(a) A bailee who takes out insurance in its own name without the knowledge of the bailor, is trustee for any excess above its claim after a loss. Here, if the plaintiff receives from the Insurance Company money representing the Northern Pacific flat car loss, such money is a trust fund entirely belonging to the Northern Pacific. In other words, under the law the Northern Pacific is immediately entitled to any money which would be paid to the plaintiff by the Insurance Company. The stipulation shows that the Northern Pacific has received that money for the loss direct

from the Insurance Company and has executed its releases. Under such circumstances, from the very nature of the rights of the parties, there is no cause of action. A case in point: *Robert Williams & Co. v. Auto Express Co.*, 78 Atl. 670 (N. J.).

We respectfully submit that the judgment entered by the lower court denying recovery to plaintiff on account of the Northern Pacific logging flat cars should be affirmed.

Respectfully submitted,

HAROLD M. SAWYER,

L. B. DAPONTE,

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Attorneys for Cross-Appellee.

APPENDIX

(For complete Memorandum Decision see Tr. 58-63;
also as reported 8 F. Supp. 394.)

“In the District Court of the United States, for the
Northern District of Washington, Northern Di-
vision.

No. 20512

GUY H. CLARK, as Receiver of the Montborne Lum-
ber Company, a corporation, Plaintiff,

vs.

NORTH RIVER INSURANCE COMPANY, a cor-
poration, Defendant.

MEMORANDUM DECISION

“ * * * As to the logging flat cars owned by the Rail-
way Company, it seems to me that in the final analy-
sis the question of defendant's liability under the pol-
icy must turn upon the effect to be given to the en-
dorsement on the policy that ‘It also understood and
agreed that this policy covers the legal liability only
of the assured on logging cars owned by others * * *’.
In the law relating to insurance as well as other con-
tracts, the rule is that specific provisions must control
over general provisions, and construing the policy,
together with said endorsement, it is obvious that
the parties intended that liability of the assured
rather than loss or damage to the insured, was the
thing insured against. By reason of the settlement

of the question of damage to the cars made direct by the defendant with the Railway Company, and the release and discharge of the Lumber Company and the plaintiff receiver by the Railway Company, controlling evidence of which may be found by a reference to 'Exhibit 3' attached to the stipulation of facts filed herein May 1, 1934, plaintiff has wholly failed to prove, what was required of him, that, as a result of the damage to the cars, assured is legally liable to the Railway Company in any sum. Plaintiff, therefore, has not sustained the burden of proof as to his claim or claims set forth in the complaint herein as to the cars, no matter on what theory, nor under what kind or nature of an insurance policy, such claim or claims may have been asserted. In fact, all of the proof on this question conclusively shows that the Lumber Company and plaintiff have no legal liability whatsoever to the Railway Company or the owner of the cars. It, therefore, is unimportant whether the policy was an indemnity, a liability, or a so-called 'fire policy,' because, as to the cars, plaintiff has proved no facts warranting recovery under any theory or under any kind of policy. On this issue as to the cars, the judgment of the court will be for the defendant. * * * "

JOHN C. BOWEN,

United States District Judge."

5
No. 7820

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

**NORTH RIVER INSURANCE COM-
PANY** (a corporation),

Appellant and Cross-Appellee,

vs.

GUY H. CLARK, as Receiver of the
Montborne Lumber Company (a cor-
poration),

Appellee and Cross-Appellant.

BRIEF OF APPELLEE AND CROSS-APPELLANT

HENDERSON & McBEE,

Attorneys for Appellee and
Cross-Appellant,

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FILED

AUG 29 1935



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GUY H. CLARK, as Receiver of the
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poration),

Appellee and Cross-Appellant.

BRIEF OF APPELLEE AND CROSS-APPELLANT

Following the example set by the appellant and cross-appellee, the appellee and cross-appellant will refer to the parties in this litigation as “plaintiff” and “defendant.”

As is stated in the opening pages of the brief for appellant and cross-appellee, two claims by the plaintiff, Montborne Lumber Company, were asserted against a policy of insurance written that company by the defendant insurance company.

One claim involved damages to a logging locomotive. The second claim involved recovery for damages to some flat cars owned by the Northern Pacific Railway.

The lower court granted the plaintiff judgment upon its cause of action on the locomotive, from which decision the defendant appealed. The lower court denied any recovery upon the cause of action for the logging flat cars, and from this decision the plaintiff cross appeals.

The opening brief served upon counsel for the appellee and cross-appellant deals only with the judgment for the value of the locomotive and this brief, being in reply, will concern itself with that question only. A separate opening brief on the question of the damaged flat cars has been written and filed in view of the fact that counsel for the Northern Pacific Railway, who have no connection with the case involving the locomotive, will write the answering brief on the cross appeal.

STATEMENT OF THE FACTS

The facts were all embodied in a written stipulation. (Tr. p. 33 to 39) and the appellee finds no fault with the statement of the facts contained on pages 2 to 5 of appellants' brief.

ARGUMENT

The policy sued upon wherein the plaintiff's predecessor in interest, the Montborne Lumber Company is the named assured reads in part as follows:

"in consideration of the stipulations herein named, and of \$630.00 premiums, does hereby insure Montborne Lumber Company * * * (Tr. p. 49) against loss or damage caused by fire, derailment or collision * * * to rolling stock as per schedule." (Tr. p. 50)

A description of the locomotive concerned in this litigation was contained in the schedule which was attached to the policy. (Tr. p. 57)

In the first instance, the court's particular attention is directed to the language of the policy, and it is to be noted that the policy is more than a mere policy of insurance against fire only, for the language of the policy provides that the named assured is insured against the

"loss or damage caused by fire * * * collapse of bridges, lightning, etc." (Tr. p. 50)

The policy is obviously what might be termed a "railroad policy."

A diligent search by counsel for both sides has failed to reveal any cause on all fours with the question before the court.

An examination and study therefore of the general

rules covering the situation must be made.

It is appellant's contention that inasmuch as the locomotive itself was not physically damaged and that the plaintiff still has its locomotive that no recovery should be allowed. This is not the law.

FIRE NEED NOT TOUCH INSURED PROPERTY

A fair statement of what damages are recoverable under a policy of fire insurance is found in **26 C. J. 340**, and reads as follows:

“In order that there may be a recovery on the policy the fire must have been the proximate cause of the loss; or in other words such loss only can be recovered as is the proximate and immediate result of the fire as distinguished from a remote loss, and proximate loss, within this rule includes not only losses which are directly caused by the fire itself, but also losses of which the fire is the efficient cause by setting in motion other agencies, but the fire must reach the thing insured, or come within such proximity to it that damage direct or indirect is within the compass of reasonable probability. Recovery may be had for the proximate loss although the insured property is brought within the peril of the fire by some outside agency. Any loss resulting from an effort to put out a fire, or otherwise save the property, whether by spoiling the goods or otherwise, directly or indirectly, is within the policy.”

To the same effect is **14 R. C. L. 1216**:

“As in marine insurance, insurers against fire are answerable for direct and immediate, but not for consequential and remote, losses from the peril insured against.”

The rule is also well stated in **6 Couch on Insurance, Sec. 1467, p. 5304:**

“So the law of insurance seeks to administer according to the fair interpretation of the intent of the parties, and deems that to be a loss, within the policy, which is a material and necessary consequence of the peril insured against. Similarly a loss by fire includes every loss necessarily following from the occurrence of a fire if it arises directly and immediately from the peril or necessarily from incidental and surrounding circumstances, the operation and influence of which could not be avoided; that is consequences naturally flowing from or incident to a peril insured against, are attributable thereto; and as already noted it is held that if the thing insured becomes directly chargeable with any expense, contribution or loss in consequence of a particular peril that peril is the proximate cause of such expense.”

To the same effect and slightly more pertinent is **14 R. C. L. 1216:**

“But to render a fire the immediate or proximate cause of loss or damage, it is not necessary that any part of the insured property should be actually ignited or consumed by fire. Insurance against loss by fire includes loss where the cause insured against was the means or agency in causing the loss, even though it was entirely due to some other active, efficient cause which made use of it or set it in motion.”

Another case announcing this rule is the case of **Ermentraut vs. the Girard Fire Ins. Co., Minn. (1895) 65 N .W. 635:**

“To render the fire the immediate or proximate

cause of the loss or damage, it is not necessary that any part of the insured property actually ignited or was consumed by fire. This is so well settled that the citation of authorities in support of the proposition is unnecessary. The question is, was the fire the efficient and proximate cause of the loss or damage.”

In the case of **Russell vs. German Fire Insurance Company, (Minn.) 10 L. R. A. (N. S.) 326, 111 N. W. 400**, this principle was also applied.

In that case, the wall of an adjoining five-story building which had been left standing after a fire in that building, fell some seven days thereafter. At that time a strong wind was blowing, the walls left standing from the building consumed by fire fell and damaged the adjoining building, and in a suit by the owner of the adjoining building against the insurance company which had the insurance upon **that** building, the lower court found that the cause of the walls falling was the fire and not the wind, and upon this finding the appellate court affirmed the judgment, using this language:

“It was at least a question of fact, and the finding of the trial court that the fire was the cause of the injury is sustained.”

And in **Western Assur. Co. vs. Hann (1917) 201 Ala. 376, 78 So. 232**, following the above Russell case, it was held that whether or not the proximate cause of the loss of a stock of goods resulting from the falling, dur-

ing a strong wind, of the wall of a building adjoining the building in which the goods were, was a fire in such building, which had taken place some four months before, and which had left such wall standing as a result thereof, was a question for the jury, the court having determined that the word "direct" as used in the policy insuring the goods "against all direct loss or damage by fire" meant nothing more than "proximate" and a finding of the jury in the affirmative was approved of, the court saying that the evidence authorized the jury to find that the fire was the proximate cause of the loss, and that the wind was but an intervenient agency, or incident in the chain of events which could reasonably have been foreseen.

Another case which is pertinent to the inquiry is the case of **Brandyce vs. U. S. Lloyds, Inc. (N. Y. 1924) 147 N. E. 201: (Also in 203 N. Y. S. 10)**

"Appeal, by permission, from a judgment of the Appellate Division of the Supreme Court in the Second Judicial Department (207 App. Div. 665, 203 N. Y. S. 10) entered January 14, 1924, in favor of plaintiffs upon the submission of a controversy under sections 546 and 547 of the Civil Practice Act. The action was to recover under a policy of marine insurance by which the defendant insured a shipment of potatoes on the steamship *Coriscana* from New York consigned to Caibarien, Cuba. The vessel struck some unknown object and was damaged to such an extent that she had to put into Charleston, S. C., to make repairs. The shipment of potatoes here involved was not injured directly

by the collision or touched sea water, but in order to make the repairs, the cargo, including the potatoes, had to be discharged and held at the port of refuge until the repairs were completed and the vessel resumed her voyage. The potatoes, being perishable, were not able to stand the delay, and on the advice of surveyors, whose conclusions are not disputed, the potatoes were sold for upwards of sixty per cent. of their sound value. It is agreed in the submission that "the only loss suffered, or which would have suffered by them, was natural deterioration" and that the vessel completed her repairs and carried out the voyage. The question involved is whether loss by natural deterioration during a delay of the voyage caused by a sea peril is a loss by sea perils. The appellate division held that the proximate cause of the loss was the sea peril and directed judgment for plaintiff."

QUESTION ONE OF CAUSATION

It is apparent from the foregoing authorities that fire need not physically touch or damage the thing insured, but that the insurer is liable if the fire is the proximate cause of the damage.

The case of **Hall vs. Great American Insurance Company, (Iowa) 1934, 252 N. W. 763** is instructive on this point.

The facts in that case were that the plaintiff was the owner of a dwelling house and household furniture which were covered by a policy of fire insurance. The policy provided that "clocks, watches and jewelry in use" were included in the policy.

The plaintiff's premises burned. The evidence show-

ed that shortly before the fire the plaintiff, who owned a diamond ring, had placed the same on the mantel in his house on the morning of the fire.

“that no one was in the house except himself, his wife, and his son from that time until the time of the fire; and that no one of these three persons removed the diamond from the mantel. While the fire was in progress, many people were in and out of the house helping remove furniture and other articles. The fire consumed the upper portion of the house, and, in trying to subdue it, the fire company used such large quantities of water that after the fire the water on the living room floor was two or three inches deep. After the fire was over the living room floor and mantel were covered with water, fallen plaster and debris, and, as soon as it was possible to enter the house after the fire, a search was commenced for the diamond, but it was not found.”

The court holds that upon this evidence the jury could well find that the diamond was lost or destroyed as a direct or proximate result of the fire in question.

Another example of the application of the rule of causation is found in the case of **Lynn Gas and Electric Company vs. Meriden Fire Insurance Company**, 158 Mass. 570, 33 N. E. 690, 20 L. R. A. 297.

The policy in that case insured a building and machinery against loss or damage by fire.

A fire occurred in the wire tower, situated some distance from the building in which the dynamos and other electrical machines of the insured were placed.

By reason of the burning of the wire tower a short circuit was formed. This caused a sudden increase of pressure upon the driving belt of the dynamo, which parted, and left the engine without restraint. The fly wheel, thus caused to revolve too rapidly, burst, and wrecked the machinery and building. It was contended by the defendant that the loss to the machinery and building was too remote to be covered by the insurance against fire. But the court held that there was an unbroken chain of causation between the fire in the tower and the wrecking of the building and machinery, and therefore held the insurer liable as for damage by fire.

An other example of the liability of an insurer for damages not physical to the property is the case of **Stag Mining Company vs. Missouri Fidelity Company, Missouri (1919) 209 S. W. 321**. In this case the plaintiff company had an employer's liability policy. A workman was injured, due to the negligence of the company, and died as a result of his injuries. His widow brought suit against the mining company and recovered a judgment for \$5,000.00. The insurance company did not pay the judgment and the widow levied execution on the property of the mining company. Certain property of the mining company was sold on execution sale for \$450.00. As a matter of fact, the reasonable market value of the property thus sold on execution was the sum of \$5,000.00.

In a suit brought by the mining company against the insurance company, the insurance company defended upon the ground that they were liable only for the \$450.00 and that they were not liable for the \$5,000.00.

The court, in deciding the liability of the insurance company to be the reasonable value of the property sold, uses the following language:

“Nor can there be any objection to fixing the amount of damages at the reasonable value of the property seized and sold because of same being uncertain and speculative. The reasonable value of the property at a given time and place is the measure of damages in trover, conversion, replevin, and a variety of actions, and such value can readily be arrived at with reasonable certainty. If the plaintiff was with reasonable certainty. If the plaintiff was claiming damages by reason of loss to its business or of future profits by reason of being deprived of the use of the mining plant and machinery seized and sold, then the defendant might well claim that such damages are consequential, remote, or speculative; but not so where plaintiff is claiming no more than the reasonable value of the property taken from it.

Turning again to the policy itself, we find that the agreement is to indemnify the assured for loss or damage by reason of legal liability, and then natural inquiry is: What did the assured lose, or how much was it damaged, by reason of the seizure and sale of this property? The question is not how much did the execution plaintiff receive, because that is not necessarily the amount which the assured lost, even when leaving out such items as court costs or attorneys' fees where same are paid by the assured. The liability of the defendant is

for the loss or damage to the assured, and not the advantage or gain to the injured employee.”

As sustaining the rule quoted from 6 Couch on Insurance, Sec. 1467, p. 5304 that all expenses flowing from or incident to a peril insured against are attributable thereto, and that if the thing insured becomes directly chargeable with any expenses that expense is recoverable against the insurance company, is the case of **Hale vs. Washington Insurance Company**, Fed. case No. 5916, 11 Fed. cases, p. 189.

The facts in this case were that an American ship carrying a policy of insurance insuring it against perils of the sea collided with a British ship in British waters. The British owners threatened to libel the American vessel. The master of the American vessel compromised with the British owner.

The American ship was also damaged in the collision.

In a suit by the owners of the American ship against the insurance company, the company defended upon the grounds that they were liable only for the physical damage to the American ship and were not liable for the sum paid in compromise to the owners of the British ship by the master of the American ship.

Mr. Justice Storey, the author of the opinion, in

holding the insurance company liable for the full amount, uses this language:

“The argument seems to suppose that the insurance attached only to the extent of the direct injury sustained by the very thing insured. But that argument is not well founded. Any and every expense borne by and chargeable upon the owner of the thing insured, and as a direct and immediate consequence of a peril insured against, is covered by the policy.

* * * The truth is that in all these and the like cases, we look to the origin of the loss. If it be a peril insured against, all the incidents and attachments thereto by law, as necessary or natural incidents become a part of the loss, just as much as the storage of goods saved from a shipwreck is deemed a part of the loss; and the expenses in court of a suit to ascertain the salvage are also deemed a part of the loss.”

The last case to which the plaintiff desires to call the court's attention in the matter is the case of **Brady vs. Northwest Insurance Company, 11 Mich. 425.**

The facts in that case were that the defendant had issued a policy of fire insurance on a frame warehouse in the city of Detroit. A fire occurred and there was some damage to the warehouse.

A city ordinance of Detroit at the time of the fire prohibited the rebuilding of wooden structures within certain areas and the warehouse was in this area.

The insurance company, in a suit by the owner of the building, defended on the grounds that they were

liable only for the value of the material damaged by the fire.

While the insured claimed that by virtue of the fire and the ordinance the building to him was a total loss, in holding the insurance company liable for a total loss, the court said:

“Under this rule, what was the plaintiff’s loss in the present case? The property insured was situated within the fire limits of Detroit, within which the reconstruction or repair of any wood building injured by fire was prohibited, unless by leave of the common council. The charter and ordinances of the city upon this subject and the refusal of the common council to permit the repair of the building injured were offered in evidence to show the extent of the plaintiff’s loss and rejected. This charter and these ordinances were in existence at the time of the last renewal of the policy. They were local laws affecting the property and the risk which the defendant assumed and of which the latter is presumed to have had knowledge and to have estimated in renewing the policy. Whether therefore in case of damage or partial loss the common council would permit a repair of the building, was a risk which the company took upon itself, because the loss and injury to the plaintiff might depend in amount upon such action of the council, while such loss and injury would be absolutely and actually the consequence of the fire; and because by the terms of the policy, the company reserved the right to repair or not at option, thus taking the risk of the power to repair, and of all loss which should accrue if repairing should be impossible from any cause. To hold that for an injury to the property which results, without the fault of the insured, in a total loss to him, so far as value and use are

concerned, the insured can only receive compensation to the extent of the appraised damage to the materials of which the building was constructed and which were destroyed would establish a narrow, illiberal and illogical rule. The value of the building consisted of its adaptation to use as well as in the materials of which it consisted; and if it could not be restored to use after the fire, the loss was total, less the value of the materials rescued. In the very pertinent language of the plaintiff's counsel, 'The contract was not simply an agreement to pay for so much material as might be damaged by fire to pay such amount as the material might actually be worth. Fixed by the conditions of the policy as the most hazardous of all structures, and with a premium adjusted accordingly, the insurer took the risk upon a three story wood warehouse actually in use as such. The risk was not taken upon a collection of beams, boards and other materials all thrown together without purpose of special adaptation. It was upon a building for trade, situate within a particular locality and within the jurisdiction of municipal authorities vested with legislative powers for special purposes and subject to the exercise of those powers;' and the parties must be regarded as having contracted with a full knowledge of all the facts and the law and the risk to which the property was thereby subjected."

The appellant argues that the logic of the case just above cited is not applicable because in that case there was an actual physical damage to the property. This argument is aptly and conclusively refuted by the language of **Hale vs. Washington Insurance Co., Fed. Cases, No. 5916, 11 Fed. Cases p. 189** where the same argument was advanced and the court said:

“the argument seems to suppose that the insurance attached only to the extent of the direct injury sustained by the very thing insured. But that argument is not well founded. Any and every expense borne by and chargeable upon the owner of the thing insured, and as a direct and immediate consequence of a peril insured against, is covered by the policy.”

To sustain appellant's contention in this respect would compel a holding to the effect that a physical damage to the locomotive must occur and that the well established rule for the determination of liability upon fire insurance policies, to-wit, that of causation, is erroneous.

This contention is also specifically negatived in **14 R. C. L. 1216:**

“But to render a fire the immediate or proximate cause of loss or damage, it is not necessary that any part of the insured property should be actually ignited or consumed by fire. Insurance against loss by fire includes loss where the cause insured against was the means or agency in causing the loss, even though it was entirely due to some other active, efficient cause which made use of it or set it in motion.”

and also in the case of **Ermentraut vs. the Girard Fire Ins. Co. (Minn. 1895, 65 N. W. 635):**

“To render the fire the immediate or proximate cause of the loss or damage, it is not necessary that any part of the insured property actually ignited or was consumed by fire. This is so well settled that the citation of authorities, in support of the proposition is unnecessary. The question is,

was the fire the efficient and proximate cause of the loss or damage.”

Other authorities to the same effect are **6 Couch on Insurance Sec. 1467, p. 5304:**

“Similarly a loss by fire includes every loss necessarily following from the occurrence of a fire if it arises directly and immediately from the peril or necessarily from incidental and surrounding circumstances, the operation and influence of which could not be avoided; that is consequences naturally flowing from or incident to a peril insured against, are attributable thereto; and as already noted it is held that if the thing insured becomes directly chargeable with any expense, contribution or loss in consequence of a particular peril that peril is the proximate cause of such expense.”

The appellant also argues that to allow a recovery under the facts in the case at bar would mean that the policy would be broadened to insure the policy holder against all damages to the rolling stock and rolling equipment which would prevent the operation of the locomotive.

It is appellee's contention that when a damage occurs, caused by a peril insured against, which renders the locomotive valueless, that the company is liable, and if a fire occurred doing damage to a bridge of \$500.00, and that on account of that damage the locomotive became valueless, that the company would be liable.

In other words, the insurer is liable for the damages sustained by the assured to its property covered by the policy and caused by fire whether fire consumed, touched or destroyed the property or not.

A case much relied on by appellant is the case of **Edgar Thompson Steel Co. vs. Boylston Mutual Insurance Company**, 120 Mo. Appeals, 244.

The subject matter of this insurance was a cargo of pig iron insured against the perils of the sea. The iron was loaded on a barge and sank. The insurance company recovered the pig iron and sent it to its destination intact, but its arrival was delayed for several days.

The assured brought suit against the company for the difference in the market value at the time when the iron arrived and the price it would have brought had it arrived on time, and the court denied recovery.

Appellant cites this case as authority for the proposition that appellee is here attempting to collect insurance on profits.

Appellee has no complaint with the decision in this case and if applying the same logic the appellant will make the same effort to comply with its contract as did the company in the cited case, appellee will have no complaint.

In other words, in the cited case, the insurance

company recovered the pig iron and sent it to its destination. If the company in the case at bar will repair the bridges so that the locomotive can be run upon appellee's railroad, appellee will have no complaint, and would have no claim for damages for the time that the locomotive had remained idle.

CONCLUSION

In conclusion it is submitted that by reason of a peril insured against, to-wit, fire, the value to the plaintiff of the locomotive is completely wiped out, that the expense of rebuilding the trestles and bridge is, in the language of the Hale case, an

“expense borne by and chargeable upon the owner of the thing insured, as a direct and immediate consequence of the peril insured against.”

and as such, is covered by the policy.

Or, in the language of the Brady case,

“the risk was not taken upon a collection of beams, boards, and other materials (in the case at bar, steel, iron and brass) thrown together without purpose of special adaptation. It was upon the building (locomotive) for trade * * * and the parties must be regarded as having contracted with a full knowledge of all the facts (including the location of the locomotive and the building) and the law and the risk to which the property was thereby subjected.” (Words in parentheses ours)

It is respectfully submitted that the cause on the

appeal of the appellant and cross appellee should be affirmed.

HENDERSON & McBEE

Attorneys for Cross Appellant
and Appellee

618 First Street,
Mount Vernon, Washington

No. 7826

United States
Circuit Court of Appeals
For the Ninth Circuit.

CALIFORNIA BARREL COMPANY, INC.,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Transcript of Record

Upon Petition to Review an Order of the United States
Board of Tax Appeals

FILED

APR 19 1935

PAUL F. O'BRIEN,
CLERK

No. 7826

United States
Circuit Court of Appeals

For the Ninth Circuit.

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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APPEARANCES :

For Petitioner:

FREDERICK C. ROHWERDER, Esq.,

T. H. LAWRENCE, Esq.,

(Withdrawn)

ALLEN G. WRIGHT, Esq.,

RANDALL LARSON, Esq.,

GEO. E. H. GOODNER, Esq.,

D. F. PRINCE, Esq.

For Respondent:

ALLIN H. PIERCE, Esq.,

IRVING M. TULLAR, Esq.

Docket No. 47419

CALIFORNIA BARREL COMPANY, INC.,
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

DOCKET ENTRIES:

1930

- Feb. 10—Petition received and filed. Taxpayer notified. (Fee paid)
Feb. 11—Copy of petition served on General Counsel.
Apr. 7—Answer filed by General Counsel.
Apr. 10—Copy of answer served on taxpayer—Circuit Calendar.

1933

- July 3—Hearing set in San Francisco, California, beginning Sept. 11, 1933.
Aug. 29—Notice of appearance of T. H. Lawrence as counsel for taxpayer filed.
Sept. 15—Hearing had before Mr. Van Fossan (assigned to Mr. Leach) on merits. Submitted to Mr. Leach for report. Stipulation of facts filed. Petitioner's brief due Oct. 14, 1933—respondent's brief due Nov. 14, 1933.
Oct. 4—Transcript of hearing of Sept. 15, 1933 filed.
Oct. 11—Motion for 15 days extension to file briefs filed by taxpayer.

1933

- Oct. 12—Motion for 15 days extension to file briefs granted to both parties.
- Oct. 30—Brief filed by taxpayer. 10/30/33 copy served on General Counsel.
- Nov. 29—Brief filed by General Counsel.
- Dec. 29—Motion for leave to file reply brief filed by taxpayer—reply brief lodged. 12/29/33 granted.

1934

- Jan. 8—Copy of reply brief served on General Counsel.
- Nov. 7—Memorandum opinion rendered—J. Russell Leech, Division 6. Judgment will be entered for the respondent.
- Nov. 8—Decision entered—J. Russell Leech, Division 6.

1935

- Jan. 4—Notice of the withdrawel of T. H. Lawrence, counsel for taxpayer, filed.
- Jan. 5—Motion to fix amount of bond filed by taxpayer.
- Jan. 5—Order fixing amount of bond at \$24,000 entered.
- Jan. 5—Notice of the appearance of Geo. E. H. Goodner and D. F. Prince, counsel for taxpayer, filed. [1]*
- Jan. 29—Notice of the appearance of Randell Larson, counsel for taxpayer, filed.
- Jan. 29—Supersedeas bond in the amount of \$24,000. approved and ordered filed.

*Page numbering appearing at the foot of page of original certified Transcript of Record.

1935

- Jan. 29—Petition for review by U. S. Circuit Court of Appeals (9) with assignments of error filed by taxpayer.
- Jan. 29—Proof of service filed.
- Jan. 29—Statement of evidence lodged.
- Jan. 29—Notice of lodgment of statement of evidence with hearing notice of Feb. 13, 1935 filed.
- Feb. 12—Motion to continue hearing to Feb. 27, 1935 filed by taxpayer. 2/12/35 granted.
- Feb. 23—Order from 9th Circuit to transmit certain original exhibits filed.
- Feb. 26—Agreed statement of evidence approved and ordered filed.
- Feb. 26—Praecipe filed with proof of service thereon.
- Mar. 26—Order enlarging time to April 15, 1935 for transmission and delivery of record entered. [2]

United States Board of Tax Appeals

Docket No. 47419

CALIFORNIA BARREL COMPANY, INC.,
Petitioner.

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

PETITION

The above named petitioner hereby petitions for a redetermination of the deficiency set forth by the

Commissioner of Internal Revenue in his notice of deficiency (IT:AR:C-1:JMK-60D), dated December 12, 1929, and as a basis for its proceeding alleges as follows:

1. The petitioner is a California corporation, with its principal office at 433 California Street, San Francisco, California.

2. The notice of deficiency (a copy of which is hereto attached and marked "Exhibit A") was mailed to the petitioner on December 12, 1929. The details resulting in the deficiency shown are set forth in a separate communication addressed to the California Barrel Co. (a copy of which is hereto attached and marked "Exhibit B") dated December 12, 1929.

3. The taxes in controversy are income and profits taxes for the calendar year 1927, and for \$14,915.65.

4. The determination of the tax set forth in the said notice of deficiency is based upon the following error:

(a) Respondent erred in failing and refusing to permit the petitioner to deduct from gross income during the calendar year 1927, the sum of \$306,-348.56, representing a net loss incurred during the calendar year 1925. [3]

5. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

(a) Petitioner is engaged in the manufacture and sale of barrels and cooperage.

(b) The amount of the net loss is not in dispute, the sole question at issue being its deductibility in the 1927 income tax return.

(c) The affairs of the California Barrel Co., incorporated January 18, 1906, hereinafter referred to as "A" company, were reorganized by the formation of a new corporation, known as the California Barrel Company, Inc., incorporated February 15, 1924, hereinafter referred to as "B" company.

(d) "B" company has an authorized capital stock of 18,000 shares, divided into 9,000 shares of preferred capital stock of a par value of \$100.00 per share, and 9,000 shares of common capital stock of no par value, only 1,000 shares of the common stock being issued. The preferred and common stock have equal voting rights.

(e) "A" company transferred on August 28, 1924, all of its net assets including goodwill to "B" company in exchange for 9,000 shares of preferred stock. 1,000 shares of common stock of "B" company were issued to "A" company's stockholders.

(f) The California Supreme Court decided on July 29, 1925 (*Del Monte Light & Power Co. v. Jordan*, 196 Cal. 448), that California corporations could not issue shares both with and without par value.

(g) In compliance with this decision, and by reason of the licensing authority of the State of California, "B" company, against its will, was compelled to reorganize and did so by reincorporating

under California laws on December 19, 1925, under the name of California Barrel Company, Inc., hereinafter referred to as "C" company. [4]

(h) On December 31, 1925, "B" company transferred all of its net assets, including goodwill, to "C" company in exchange for 9,000 shares of preferred, and 250 shares of common stock, both of \$100.00 par value and with equal voting rights. The "C" company common stock was issued pro rata to the "B" company common stockholders, and the preferred stock to "A" company.

(i) Except for the retirement of 270 shares of "C" company preferred stock on September 30, 1936, no change has occurred in "A" company's ownership in "C" company.

(j) "A", "B", and "C" companies are and always have been close corporations controlled by the Koster family.

(k) For the calendar year 1925, "A" and "B" company filed separate income tax returns. "A" company reported \$13,500.00 dividends received from "B" company and had no other income or expenses. "B" company reported a loss of \$504,572.66, which after deducting \$70,000 received in dividends, made a statutory net loss of \$504,502.66.

(l) For the calendar years 1926 and 1927, "A" and "C" companies filed consolidated income tax returns.

(m) In the 1927 consolidated tax return, there was deducted the amount of \$306,348.56 represent-

ing the portion of "B" company's 1925 statutory net loss in excess of the 1926 consolidated net income.

6. Wherefore, the petitioner prays that this Board may hear the proceeding and determine that the taxpayer is entitled, in computing its net income for the calendar year 1927, to deduct the amount of \$306,348.56.

(Signed) FREDERICK C. ROHWERDER

(Signed) ALLEN G. WRIGHT

Counsel for Petitioner.

February 5th, 1930. [5]

State of California,

City and County of San Francisco—ss

F. J. KOSTER, being duly sworn, says that he is the President of California Barrel Company, Inc., the petitioner named in the foregoing petition, and as such is duly authorized to verify the foregoing petition; that he has read the foregoing petition or had the same read to him, and is familiar with the statements contained therein and that the facts therein stated are true.

(Signed) F. J. KOSTER

Subscribed and sworn to before me this fifth day of February, 1930.

(Signed) M. V. COLLINS

Notary Public in and for the City and County
of San Francisco, State of California [6]

EXHIBIT A

COPY

TREASURY DEPARTMENT
WASHINGTON

SEAL

Office of
Commissioner of Internal Revenue

Address reply
Commissioner of Internal Revenue
And refer to

IT:AR:C-1

JMK-60D

Dec. 12, 1929.

California Barrel Company, Inc.,
433 California Street,
San Francisco, California.

Sirs:

In accordance with Section 274 of the Revenue Act of 1926, you are advised that the determination of your tax liability for the year 1927, discloses a deficiency of \$14,915.65, as shown in the statement attached.

The section of the law above mentioned allows you to petition the United States Board of Tax Appeals within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of

this letter for a redetermination of your tax liability.

HOWEVER, IF YOU DO NOT DESIRE TO PETITION, you are requested to join in executing the consolidated Form 866 enclosed in a separate communication of even date addressed to California Barrel Company, 433 California Street, San Francisco, California. The signing of this agreement will expedite the closing of your return by permitting an early assessment of any deficiencies and preventing the accumulation of interest charges, since the interest period terminates thirty days after filing the agreement form, or on the date assessment is made, whichever is earlier; WHEREAS IF NO AGREEMENT IS FILED, interest will accumulate to the date of assessment of the deficiencies.

Respectfully,

ROBT. H. LUCAS,

Commissioner.

(Signed) By DAVID BURNET

Deputy Commissioner.

Enclosures:

Statement

Form 882 [7]

COPY

IT:AR:C-1

JMK-60D

STATEMENT OF RETURNS EXAMINED.

Company	Year	Form
California Barrel Company, Inc., 433 California Street, San Francisco, California.	1927	1122
		Filed with Consolidated return of California Barrel Company.

Tax Liability.

California Barrel Company, Inc.,

Year	Corrected Tax Liability	Tax Previously Assessed	Deficiency
1927	\$14,915.65	None	\$14,915.65

Full details resulting in the deficiency shown are contained in a separate communication addressed to California Barrel Company. [8]

EXHIBIT B

COPY

TREASURY DEPARTMENT
WASHINGTON

SEAL

Office of
Commissioner of Internal Revenue

Address reply to
Commissioner of Internal Revenue
And refer to

Dec. 12, 1929.

IT:AR:C-1

JMK-60D

California Barrel Company,
433 California Street,
San Francisco, California.

Sirs:

You are advised that the determination of your tax liability for the year 1927, discloses no additional tax due as shown in the attached statement.

In accordance with Section 274 of the Revenue Act of 1926, the Bureau has advised the company against which a deficiency is shown in the attached statement of its right to petition the United States Board of Tax Appeals within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of the letter, for a redetermination of its tax liability.

If you acquiesce in the findings of the Unit, you

are requested to join in executing the enclosed Consolidated Form 866.

Respectfully,
 DAVID BURNET,
 Deputy Commissioner.
 (Signed) By H. B. ROBINSIN.
 Head of Division.

Enclosures:

Statement
 Form 866-CR
 Schedules 1 to 4, incl. [9]

COPY

IT:AR:C-1

JMK-60D

STATEMENT OF RETURNS EXAMINED

Company	Year	Form
California Barrel Company, 433 California Street, San Francisco, California.	1927	1120 (Consolidated)

California Barrel Company, Inc., San Francisco, California.	1927	1122
--	------	------

Tax Liability
 California Barrel Company, Inc.

Year	Corrected Tax Liability	Tax Previously Assessed	Overas- sessment	Deficiency
1927	\$14,915.65	None	None	\$14,915.65

Full details resulting in the deficiency shown above are disclosed in attached Schedules 1 to 4, inclusive.

Your protest of July 11, 1929, against the findings disclosed in Bureau letter of June 13, 1929, has been considered in connection with a conference held in San Francisco, California, August 13, 1929, and your protest of October 17, 1929, has been considered in connection with a conference held in Washington, D. C., November 8, 1929, but your contentions are not conceded by this office.

The deficiency shown above has been allocated to California Barrel Company, Inc., the company disclosing taxable income. [10]

COPY

California Barrel Company,

Year ended December 31, 1927.

Schedule 1

Net Income

Net loss as disclosed by consolidated	
return	\$39,060.00
As corrected—loss	39,060.00
	<hr/>
Net adjustment	No change

Schedule 2

California Barrel Company, Inc.

Net Income

Net loss as disclosed by consolidated return	\$156,802.23
As corrected—income	149,546.33
	<hr/>
Net adjustment	\$306,348.56
Unallowable deductions and additional income:	
(a) Prior year's loss	\$306,348.56

Schedule 2-A

Explanation of Items Changed

- (a) California Barrel Company, incorporated January 18, 1906, and California Barrel Company, Inc., incorporated December 19, 1925 (continuation of California Barrel Company, Inc., incorporated February 15, 1924), has each been ruled not affiliated for the year 1925.

For the year 1925 each company, California Barrel Company and California Barrel Company, Inc., filed separate returns. For the years 1926 and 1927 these companies filed consolidated returns and they have been ruled affiliated for 1926 and 1927. The Bureau holds that the net loss of the California Barrel Company, Inc., (incorporated February 15, 1924) for the year 1925 of \$306,348.56, cannot be allowed against the gross income for 1927 since

16 *California Barrel Company, Inc., vs.*

different taxable entities existed in these years due to the fact that different corporations composed the affiliated group in each year. [11]

COPY

California Barrel Company.

Year ended December 31, 1927.

Schedule 3.

Consolidated Net Income.

Net Income corrected:

California Barrel Company, Inc.	\$149,546.33
---------------------------------	--------------

Net loss corrected:

California Barrel Company.	39,060.00
----------------------------	-----------

Consolidated net income	\$110,486.33
-------------------------	--------------

Schedule 4.

Computation of Income Tax.

Consolidated Net Income	\$110,486.33
-------------------------	--------------

Income tax 13½%	14,915.65
-----------------	-----------

Previously assessed	None
---------------------	------

Additional tax to be assessed	\$14,915.65
-------------------------------	-------------

[Endorsed]: Filed Feb. 10, 1930. [12]

[Title of Court and Cause.]

ANSWER

Now comes the Commissioner of Internal Revenue, the respondent herein, by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, and for answer to the petition heretofore filed in this appeal, admits and denies as follows:

1. Admits the allegations contained in paragraph 1 of the petition.

2. Admits the allegations contained in paragraph 2 of the petition.

3. Admits the allegations contained in paragraph 3 of the petition.

4 (a). Denies that the respondent committed the errors alleged in paragraph 4 (a) of the petition.

5 (a). Admits the allegations contained in paragraph 5 (a) of the petition.

5 (b). Denies the allegations contained in paragraph 5 (b) of the petition.

5 (c) to (l); inclusive. For lack of information upon which to base a belief denies the allegations contained in subparagraphs (c) to (l), inclusive, of paragraph 5 of the petition.

5 (m). Admits that in the return of the petitioner for the year 1927 there was deducted from gross income the sum of \$306,348.56 as a portion of an alleged net loss of another corporation for the year 1925. Denies the remaining allegations contained in paragraph 5 (m). [13]

Denies generally and specifically each and every allegation contained in the petition not hereinbefore expressly admitted, qualified or denied.

WHEREFORE it is prayed that the petition be denied.

(Signed) C. M. CHAREST
General Counsel, Bureau of Internal Revenue.

OF COUNSEL:

L. W. CREASON,
Special Attorney,
Bureau of Internal Revenue.

[Endorsed]: Filed April 7 1930. [14]

[Title of Court and Cause.]

T. H. Lawrence, Esq., and Allen G. Wright Esq.
for petitioner.

Allin H. Pierce, Esq., and Irving M. Tullar, Esq.,
for respondent.

MEMORANDUM OPINION.

LEECH; This proceeding seeks redetermination of an asserted income tax deficiency of \$14,915.65 for the calendar year 1927.

Petitioner assigns as error the respondent's disallowance of a deduction of \$306,348.56 as a net loss incurred during the year 1925. The amount of the alleged net loss is also in issue.

The parties have stipulated the facts out of which the controversy arises. We set forth only those

facts sufficient for a determination of the principal issue, namely, whether petitioner is entitled to the deduction claimed.

All three corporations involved in the transactions hereinafter set forth were organized under the laws of California for the purpose [15] of engaging in the manufacture and sale of barrels and cooperage.

California Barrel Co. (hereinafter referred to as "A" company) was organized in 1906.

California Barrel Company, Inc., (hereinafter referred to as "B" company) was organized on February 15, 1934, for a term of 50 years, with a capital structure of 9,000 shares of voting preferred stock of \$100 par value each, and 9,000 shares voting common stock of no par value. Under date of August 28, 1924, the "A" company, pursuant to authority of its directors, stockholders and creditors, transferred all of its business, assets, goodwill, etc., to the "B" company which issued therefor 9,000 shares of preferred stock to "A" company, 995 shares of common stock to the stockholders of "A" company as the latter's nominees, and 5 shares of common stock, as qualifying shares, to the incorporators and directors of "B" company, who were also the directors of "A" company. The remaining authorized capital stock of "B" company was not issued. The "B" company assumed all of the liabilities of "A" company, except certain debts arising out of the latter's liability as a stockholder of a certain insolvent corporation. The transaction

was entered into for the purpose of paying such debts, and upon receipt of "B" company's stock, "A" company executed a trust agreement for the benefit of its remaining creditors. The "A" company continued its corporate existence and paid its annual franchise taxes. [16]

On July 29, 1925, the Supreme Court of California in *Del Monte Light & Power Co. v. Jordan*, 196 Cal. 488; 238 Pac. 710, held that, pursuant to the State Constitution and Civil Code, the preferred and common shares of a California corporation must have the same par value, and that such must be required of those seeking to organize a corporation or to amend the articles of corporations already organized. Following that decision, "B" company tendered to the Secretary of State of California, amended Articles providing that its no par value common stock should have a par value of \$100 per share, as did its then outstanding preferred shares. The Secretary of State refused to permit the filing of such amendment, and subsequently, in December, 1925, he refused to issue to "B" company the required statutory license to do business for the year 1926, although the prescribed license fee was tendered.

Under date of December 10, 1925, the "B" company sold certain assets transferred to it by "A" company (namely stock of the Koster Products Company) at an alleged loss of \$846,461.85, resulting in an alleged net loss of \$504,572.66 for the taxable year 1925.

To provide a means for continuing the business during 1926, the "B" company caused to be organized on December 19, 1925, for a term of 50 years, the California Barrel Company, Inc., (hereinafter [17] referred to as "C" Company) the petitioner herein. The "C" company's authorized capital stock consisted of 9,000 shares of preferred and 9,000 shares of common stock, both of the par value of \$100 each and both having voting rights.

A deed of conveyance, executed on December 29, 1925, by "B" company as first party and grantor, by "A" company as second party, and by "C" company as third party and grantee, transferred as of December 31, 1925, all of "B" company's assets to "C" company. In consideration therefor, "C" company assumed all of "B" company's liabilities and issued its capital stock as follows: 9,000 shares of preferred stock to "A" company; 125 shares of common stock to F. J. Koster; 125 shares of common stock to B. J. Critcher as trustee for the stockholders of "A" company other than F. J. Koster, and 5 shares of common stock, as qualifying shares, to its incorporators and directors. The remaining authorized capital stock of "C" company was not issued. It is stipulated that: "No steps have been taken to dissolve the "B" company and no decree of court dissolving the same has ever been entered."

Upon receipt of "C" company's stock, the "A" company executed a new trust agreement for the benefit of its creditors. Except for the retirement on September 30, 1926, of 270 shares of preferred

stock held by the "A" company, no change has occurred in its stock ownership of "C" company's stock. [18]

The "A", "B" and "C" companies each filed a separate tax return for the year 1925. The "A" company and "C" company filed consolidated returns for the years 1926 and 1927, but neither company applied for nor received, from the Commissioner of Internal Revenue, formal permission to file such returns for those years. On its return for the calendar year 1925, the "B" company reported a net loss of \$504,572.66. The "B" company filed no returns for the years 1926 and 1927. On the consolidated return filed by "A" and "C" companies for the calendar year 1927, the "C" company (petitioner herein) claimed a statutory net loss deduction in the amount of \$306,348.56 as a portion of the alleged net loss reported on "B" company's return for the year 1925. In determining the deficiency in controversy, the respondent disallowed such deduction on ground that the alleged net loss was not sustained by this petitioner.

The facts and contentions here involved are similar to those in *New Colonial Ice Co. Inc. v. Helvering*, 292 U. S. 435, decided subsequent to the submission of this proceeding. There the Court was construing sec. 204 (b) of the Revenue Act of 1921, which, for all intents and purposes, is the same as sec. 206 (b) of the Revenue Act of 1926, the applicable provision here. After stating that the extent of deductions from gross income depends upon leg-

islative grace; [19] that only as a clear provision therefor can any particular deduction be allowed; and that the income tax statutes disclose a general purpose to confine allowable losses to the taxpayer sustaining them, the Supreme Court held that the section is free from ambiguity and clearly means that the deduction shall be allowed only to the taxpayer who sustained the net loss. The Court held that the new corporation was not, for all practical purposes, the same as the old one, regardless of the continuity of the business, stockholders and creditors. The old corporation was deserted and the new one regarded as a distinct entity free from the difficulties attending the old one. In law and in fact the two corporations were distinct, since the transaction was voluntary and contractual, not by operation of law. It was then concluded that the two corporations were not the same taxpayer.

Upon authority of *New Colonial Ice Co. Inc.*, *supra*, we hold that petitioner, the "C" company, is not entitled to a deduction in 1927 for any portion of a net loss sustained in 1925 by its predecessor, the "B" company. This conclusion obviates the necessity of determining the correct amount of the alleged net loss sustained by "B" company.

Enter:

ENTERED: Nov. 7, 1934

Judgment will be entered for the Respondent.

[20]

United States Board of Tax Appeals
Washington

Docket No. 47419

CALIFORNIA BARREL COMPANY, INC.

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION

Pursuant to the determination of the Board, as set forth in its memorandum opinion, entered November 7, 1934, it is

ORDERED and DECIDED: That there is a deficiency of \$14,915.65 for the year 1927.

[Seal] (Signed) J. RUSSELL LEECH
Member.

Enter:

ENTERED Nov. 8, 1934. [21]

[Title of Court and Cause.]

PETITION OF CALIFORNIA BARREL COMPANY, INC., A CORPORATION, FOR REVIEW BY THE UNITED STATES CIRCUIT COURT OF APPEALS, NINTH CIRCUIT, OF DECISION OF THE UNITED STATES BOARD OF TAX APPEALS

To the Honorable the Judges of the United States Circuit Court of Appeals, Ninth Circuit:

Now comes California Barrel Company, Inc., a corporation, the petitioner in this cause, by Allen

G. Wright and Randell Larson, its attorneys, and respectfully shows:

I.

JURISDICTION FOR REVIEW

The petitioner, California Barrel Company, Inc., is a corporation duly organized and existing under and by virtue [22] of the laws of the State of California with its principal office in San Francisco, California. The respondent in this cause is the duly appointed, qualified and acting Commissioner of Internal Revenue of the United States, holding his office by virtue of the laws of the United States. The income tax returns of the petitioner for the calendar year 1927, being the taxable year involved herein, were filed with the Collector of Internal Revenue for the First District of California on or about the 15th day of March, 1928 and the office of said Collector then was and now is located in San Francisco, California, within the Judicial Circuit of the United States Circuit Court of Appeals for the Ninth Circuit.

This petition is filed in pursuance of the provisions of Sections 1001, 1002 and 1003, of the Act of Congress approved on the 26th day of 1926 entitled the Revenue Act of 1926 as amended by the Revenue Act of 1928 and the Revenue Act of 1932.

The petitioner is aggrieved by a decision of the United States Board of Tax Appeals rendered November 8, 1934 in the appeal of the California Barrel Company, Inc., v. Commissioner of Internal

Revenue Docket No. 47419 and determining a deficiency in income and profits taxes for the calendar year 1927 in the sum of Fourteen Thousand Nine Hundred and Fifteen and 65/100 Dollars (\$14,915.65) and the petitioner respectfully submits its petition for a review thereof by the United States Circuit Court of Appeals, Ninth Circuit.

II.

NATURE OF THE CONTROVERSY [23]

The California Barrel Co. a corporation organized and existing under the laws of the State of California, hereinafter called the "A" company, had prior to August 28, 1924 acquired 8,000 shares of the capital stock of the Koster Products at a total cost of \$908,201.85. On August 28, 1924 the "A" company transferred all its assets and business to the California Barrel Company, Inc., a corporation organized February 15, 1924, and existing under the laws of the State of California hereinafter called the "B" company, including said 8,000 shares of the capital stock of the Koster Products, in consideration of the issue of 9,000 shares of the preferred stock of the "B" company to the "A" company and the issue of 995 shares of the common stock of the "B" company to the stockholders of the "A" company, as its nominees. No other stock was ever issued by the "B" company except 5 shares of common stock as qualifying shares to the directors of the "B" company who were also directors of the "A" company. The circumstances of this transfer made of the transaction a reorganization

within the meaning of Section 203 (h) (1), (B) and (i) of the Revenue Act of 1924, in which no taxable gain or loss could be recognized. Subsequently and prior to December 10, 1925 the "B" company acquired 50 additional shares of the capital stock of the Koster Products Company at a cost of Two Thousand Five Hundred Dollars (\$2500.00). On December 10, 1925 the "B" company sold its 8050 shares of the capital stock of the Koster Products Company for Sixty-four Thousand Four Hundred Dollars (\$64,400.00) taking a loss thereon of Eight Hundred [24] Forty-three Thousand Eight Hundred and One and 85/100 Dollars (\$843,801.85). A portion of this loss was asserted by the "B" company as a net loss during the year 1925. Had the "B" company continued its corporate activities in the years 1926 and 1927 it would have been entitled under authority of Section 206 (b) of the Revenue Act of 1926 to assert as a net loss in 1926 the portion of this loss which had not been asserted as a net loss in 1925 and in addition under authority of the section noted above any portion of this loss which had not been asserted as net losses in 1925 and 1926 could have been asserted by the "B" company as a net loss in 1927. It is the right to assert a portion of this loss as a net loss for the year 1927 which has been denied by the Board of Tax Appeals in its decision, the review of which is hereby petitioned.

The taxpayer, asserting a portion of this loss as a net loss in 1927 is not technically the 'B' com-

pany, but the California Barrel Company, Inc. subsequently incorporated under the laws of the State of California, December 19th, 1925, hereinafter referred to as the "C" company. The "B" company and the "C" company were both organized under the laws of the State of California for the purpose of engaging in the manufacture and sale of barrels and cooperage. Both companies had the same stockholders holding preferred and common stock therein in substantially like proportions, and both were invested with like corporate powers in their articles of incorporation. The preferred stock of each had like preferences. The officers of [25] both companies were the same and the directors of both companies were the same except that for a matter of three months the Secretary of the "C" company substituted as a director of the "C" company for Krohn a director of the "B" company.

The "B" company transferred all its business and assets to the "C" company as of December 31, 1925 for shares of stock of the "C" company issued to the nominees of the "B" company, and in 1926 and 1927 the business of manufacturing and selling barrels and cooperage formerly conducted by the "B" company in 1925 was conducted by the "C" company with the assets of the "B" company so transferred to the "C" company December 31, 1925. The continuity of the business was not broken by this transfer from the "B" company to the "C" company and for all practicable purposes the "B"

company and the "C" company were identical and the same taxpayer.

The "C" company was organized by the "B" company on December 19, 1925 solely to provide a means for continuing the business enterprise of the "B" company during 1926 and succeeding years and for no other purpose. The organization of the "C" company and the transfer to it of the assets and business of the "B" company became necessary because the Secretary of State of California acting on an erroneous opinion of the Attorney General of California as to the law refused to recognize the "B" company as a corporation either de jure or de facto and refused accordingly to file its amended articles of incorporation when tendered in the latter half of 1925 which had been amended to conform to [26] the decision of the Supreme Court of the State of California in *Del Monte Light & Power Co. v. Jordan*, 196 Cal. 488, 238 Pacific 710, and refused to issue to the "B" company a license to do business as a corporation in 1926 as required by the provisions of the California Statutes (Stats. 1915, p. 422, Chap. 190, Stats. 1917, p. 371, Chap. 215) when the amount of the tax for such a license were tendered him in due season in December 1925 and he refused to receive the tax so tendered. By the provisions of the California Statutes a failure to pay this license tax made the corporate rights, privileges and powers of a domestic corporation, like the "B" company, suspended and incapable of being exercised. When the rights, privileges and

powers of a corporation were so suspended the statute provided that every person who attempted or purported to exercise any of the rights, privileges or powers of such a corporation was guilty of a misdemeanor and punishable by substantial fine or by imprisonment or by both and every contract made in violation of this statute, the statute itself expressly made void. It was in order to meet the foregoing situation that the "B" company organized the "C" company on December 19, 1925 and transferred its business and assets as of December 31, 1925.

The "B" company had been organized in 1924 with a capital stock whose preferred shares had a par value of \$100 each and common shares without a par value in conformity with certain sections of the California Civil Code (290 b, 290 c, 290 d, 290 e, and 290 f, added to the code in 1923; Stats. 1923 p. 621, Chap. 293). These sections of the Civil Code authorizing [27] the organization of corporations with a capital stock, some of which might have a par value and some of which might have no par value, were held to be unconstitutional under the California Constitution in the case of *Del Monte Light & Power Co. v. Jordan*, *supra*. But the "B" company was, notwithstanding that decision, at least a *de facto* corporation and as such it had the right, as it attempted, to amend its articles of incorporation to provide for a capital stock of preferred and common stock both with a par value of \$100 each to conform to that decision and as a *de facto* cor-

poration the "B" company had the right to have a license to do business during 1926 issued to it upon the tender which it made of the amount of the license tax prescribed therefor. Both rights were improperly and without warrant of law denied the "B" company, by the California Secretary of State as was later settled in 1926 in a case affecting a de facto corporation organized with a capital stock structure similar to that of the "B" company by the decision of the Supreme Court of California in *Westlake Park Investment Co. v. Jordan*, 198 Cal. 609, 246 Pac. 807.

Facing this predicament, and in order to avoid a disruption of its business from and after January 1, 1926, in order to avoid possible litigation over its future contracts, in order to void placing itself and its officers and employees in possible jeopardy of the penalties prescribed by the corporation licensing Statute of California, in order to continue its business enterprise, to protect its private rights, to safeguard the interest of its stockholders and creditors and to conserve its property interests, [28] and to avoid the expense, delay and uncertainty of likely litigation, the "B" company was forced in December 1925 to do something to meet that situation and it accordingly provided for the creation of the "C" company and the transfer of its assets and business to the "C" company as of December 31, 1925 as the only safe, certain and prompt solution of the problem with which it was confronted.

The question which has been raised as to the

right of the taxpayer, the "C" company, to assert the net loss in 1927 which it did assert in its 1927 income tax return, could never have arisen if the California Secretary of State had not, without warrant of law, denied to the "B" company its right to file with him its amended articles of incorporation and denied to the "B" company its right to a license to do business in 1926 when in due season it tendered him the prescribed license tax therefor.

The controversy in this case involves a question of law. The case was tried and submitted before the Board of Tax Appeals on an agreed statement of facts. A question was raised over what was the correct amount of the net loss sustained by the "B" company in 1925, but this question was not determined by the Board of Tax Appeals and, in the event of a reversal of the decision of the Board of Tax Appeals, which, upon the authority of the decision of the Supreme Court in *New Colonial Ice Company v. Helvering*, 292 U. S. 435, 54 Sup. Ct. 788, held that the "C" company was not entitled to a deduction in 1927 for any portion of a net loss sustained in 1925 by the "B" company, this case will probably have to be remanded to the Board of Tax Appeals for rehearing. [29]

The issue here is whether this case comes within the recognized exception to the general rule declared in *New Colonial Ice Co. v. Helvering*, *supra*, and whether or no, under the exceptional situation in this case, looking through form to substance, the substantial identity of the "B" company and the

“C” company and their identity as the same taxpayer should be recognized and whether or no that substantial identity should be recognized for the due protection of private rights, and whether, accordingly, the taxpayer, the “C” company, should or should not be permitted to assert the net loss for 1927 as claimed. The petitioner herein asserts the affirmative of this issue.

III.

ASSIGNMENTS OF ERROR

The petitioner, hereinafter referred to as the taxpayer, says that in the record and proceeding before the United States Board of Tax Appeals and in the decision and order determining a tax deficiency of \$14,915.65 rendered and entered by the United States Board of Tax Appeals manifest error occurred and intervened to the prejudice of the taxpayer. The taxpayer assigns the following errors and each of them which it avers occurred in the said record, proceeding and order of determination of said deficiency and upon which it relies to reverse said decision and order of determination of said deficiency so rendered and entered by the United States Board of Tax Appeals, hereinafter referred to as the Board, to-wit:

(1) The Board erred in making and entering its decision in this cause and in entering judgment in favor of the [30] Commissioner and against taxpayer.

(2) The Board erred in its conclusions of law and its application of the law to the facts.

(3) The Board erred in that the opinion, decision and order of the Board are contrary to the evidence and are not supported by the evidence.

(4) The Board erred in that the opinion, decision and order of the Board are contrary to the facts stipulated in this case and are not supported by the facts stipulated in this case.

(5) The Board erred in determining a deficiency against this taxpayer for the year 1927 amounting to \$14,915.65.

(6) The Board erred in holding that the taxpayer hereinabove referred to as the "C" company was not entitled to a deduction in 1927 for any portion of a net loss sustained in 1925 by its predecessor hereinabove referred to as the "B" company.

(7) The Board erred in finding that the two corporations hereinabove referred to respectively as the "B" company and the "C" company were in fact distinct corporations.

(8) The Board erred in concluding that the said "B" company and "C" company were in law distinct corporations.

(9) The Board erred in concluding that the said "B" company and "C" company were not one and the same taxpayer.

(10) The Board erred in failing to find or conclude that there is no income tax due from the taxpayer for 1927. [31]

(11) The Board erred in not accepting and stating as its findings of fact all the facts stipulated in this case as the basis for its said opinion, decision and order.

(12) The Board erred in that the opinion and decision of the Board, based upon the facts stipulated in this case, are contrary to law.

WHEREFORE, the taxpayer petitions that the decision of the United States Board of Tax Appeals be reviewed by the United States Circuit Court of Appeals for the Ninth Circuit and that a transcript of the record be prepared in accordance with law and with the rules of said Court and transmitted to the Clerk of said Court for filing, and that appropriate action be taken to the end that the errors complained of be reviewed and corrected by said Court.

ALLEN G. WRIGHT

RANDELL LARSON

1012 Mills Building

San Francisco, California

Counsel for Taxpayer-Petitioner [32]

State of California

City and County of San Francisco—ss.

FREDERICK J. KOSTER, being first duly sworn, deposes and says:

That he is the president of the California Barrel Company, Inc., the petitioner in the above named cause, and that as such president he is authorized to

verify the foregoing petition for review, and verifies the same for and on behalf of said petitioner; that he has read the said petition and is familiar with the statements contained therein and that the statements contained therein are true of his own knowledge, except as to those matters therein stated on information or belief, and as to those matters he believes them to be true.

FREDERICK J. KOSTER

Subscribed and sworn to before me this 18th day of January, 1935.

[Seal]

KATHRYN E. STONE

Notary Public in and for the City and County
of San Francisco, State of California.

My Commission Expires March 1, 1937

[Endorsed]: Filed Jan. 29, 1935 [33]

[Title of Court and Cause.]

NOTICE OF FILING PETITION FOR
REVIEW

To Robert H. Jackson, General Counsel, Bureau of
Internal Revenue, Washington, D. C.

PLEASE TAKE NOTICE that the petitioner on the 28th day of January, 1935, filed with the Clerk of the United States Board of Tax Appeals at Washington, D. C., a petition for review by the United States Circuit Court of Appeals for the

Ninth Circuit of the decision of the Board heretofore rendered in the above entitled cause. A copy of the petition for review and the assignment of errors as filed is hereto attached and served upon you. DATED at Washington, D. C. this 28th day of January, 1935.

Respectfully

ALLEN G. WRIGHT
RANDELL LARSON

Counsel for Petitioner
1012 Mills Building
San Francisco, California

[34]

Personal service of the foregoing notice together with a copy of the petition for review and assignments of error mentioned therein is hereby acknowledged this 28th day of January, 1935.

ROBERT H. JACKSON
Assistant General Counsel, Bureau of Internal
Revenue, Counsel for Respondent

[Endorsed]: Filed Jan. 29, 1935 [35]

[Title of Court and Cause.]

STATEMENT OF EVIDENCE

Following is a statement of evidence submitted to the United States Board of Tax Appeals in the above mentioned case, so far as is necessary to the

assignment of error as filed, reduced to narrative form.

This cause came on for hearing before the Honorable Ernest H. Van Fossan, Member of the United States Board of Tax Appeals, on September 15, 1933, at San Francisco, California. Allen G. Wright, Esq., appeared for the petitioner and Allin N. Pierce Special Attorney Bureau of Internal Revenue, and E. Barrett Prettyman General Counsel Bureau of Internal Revenue, appeared for the respondent.

The cause was submitted on an agreed statement of facts and Exhibit 1 attached thereto and on Exhibits 2, 3, [36] 4, 5, 6 and 7 referred to therein, and attached thereto, and duly filed with said Board.

Exhibit 2 is the separate return for 1924 of the corporation hereinafter referred to as the "B" company, Exhibit 3 is the separate return for 1925 of the corporation hereinafter referred to as the "A" company, Exhibit 4 is the separate return for 1925 of said "B" company, Exhibit 5 is the separate return for 1925 of the corporation hereinafter referred to as the "C" company, Exhibit 6 is the consolidated return for 1926 of said "A" company and said "C" company, and Exhibit 7 is the consolidated return for 1927 of said "A" company and said "C" company.

The agreed statement of facts designated as a Stipulation of Facts and Exhibit 1 attached thereto was in the words and figures following, to-wit:

STIPULATION OF FACTS

1. Petitioner is a corporation organized under the laws of California on December 19, 1925. During the years 1926 and 1927 it was engaged in the manufacture and sale of barrels and cooperage with principal offices at 433 California Street, San Francisco. During the taxable year 1927 it claims the right to deduct from its income, for Federal Tax purposes, an alleged statutory net loss resulting from the following facts which the parties hereto stipulate and agree to be true and correct: [37]

2. California Barrel Co. (in the petition and hereinafter referred to as the "A" company) was incorporated January 18, 1906, under the laws of the State of California for the purpose of engaging in the manufacture and sale of barrels and cooperage. During the year 1910 it acquired certain timber lands in the State of Oregon; and in 1918 it acquired certain other timber lands in the State of Washington. In the year 1918 it improved and equipped the Oregon lands with a railroad, logging equipment, machinery, etc. The adjusted cost of certain properties to the "A" company as of May 31, 1919, was as set forth in Exhibit 1 attached hereto and incorporated herein by reference.

3. On May 31, 1919, the "A" company transferred all of the foregoing properties, including plant and timber lands to the Koster Products Company, a corporation organized under the laws of the State of Nevada, in consideration for the issuance to

it by the latter company, of 3,000 shares of the common capital stock of the Koster Products Company, having a par value of \$100.00 per share; plus promissory notes of the said Koster Products Company in the sum of \$250,000.00. At the time received, the fair market value of the common capital stock of the Koster Products Company established by sales of said stock made to other parties was \$50.00 a share.

4. Following the said transfer, the Koster Products Company set up on its books, the assets received from the "A" company at a cost of \$400,000.00.

5. Prior to the transfer above mentioned, the "A" [38] company did not own any of the stock of the Koster Products Company. Immediately following the above mentioned transfer, the stock of the Koster Products Company was owned, as follows:

	Shares
California Barrel Co. ("A" company)	3,000
Stockholders of the "A" company	400
Non-stockholders of the "A" company	160
	<hr/>
Total	3,560

6. In November, 1919, the promissory note of the Koster Products Company which was delivered to the "A" company as part consideration for the said transfer of properties above referred to was paid by delivery to the "A" company by the Koster Products Company of 5,000 shares of the common capital

stock of the Koster Products Company at an agreed price of \$50.00 per share. Following said transaction, the 8,000 shares of the capital stock of the Koster Products Company was set up on the books of the "A" company at a total cost of \$400,000.00. There were no other changes in the stockholdings of the Koster Products Company.

7. On February 15, 1924, Articles of Incorporation of the California Barrel Company, Inc. (in the petition and hereinafter referred to as the "B" company) were filed with the Secretary of State of the State of California, who thereupon issued to the "B" company, a certificate under the seal of said state of the incorporation thereof. The purposes of the "B" company as provided for in these Articles of Incorporation were to engage in the manufacture and sale of barrels and cooperage. These Articles of Incorporation provided that the capital stock [39] of the "B" company was to consist of 18,000 shares, divided into 9,000 shares of preferred capital stock of a par value of \$100.00 per share, and 9,000 shares of common capital stock of no par value, both the preferred and common stock having voting rights. These Articles of Incorporation made provision for the preferences of the preferred stock and in that behalf made provision for accumulated dividends thereon at rates therein specified, for their redemption at par and unpaid accrued dividends and for a sinking fund plan to provide for their redemption. These Articles of Incorporation also provided that the holders of

the preferred stock in case of liquidation, dissolution or winding up were to be paid in value, both the par value of their stock and unpaid accrued dividends thereon before the payment of any amount to the holders of the common stock, and provided further that the holders of the common stock should not be entitled to receive any dividends thereon while any of the preferred shares were issued and outstanding, without the written consent of the holders of at least three-fourths of the issued and outstanding preferred shares.

8. Under date of August 28, 1924, the "A" company, pursuant to authorization of its directors and stockholders and all of its creditors, transferred to the "B" company all of its business and properties, including real estate, personal property, going concern value, goodwill, etc., and including the above mentioned 8,000 shares of the common capital stock of the Koster Products Company, in consideration of the issuance to the "A" company by the "B" company of 9,000 shares of its preferred [40] capital stock, and at the same time 995 shares of common capital stock of the "B" company issued to the stockholders of the "A" company as its nominees. At the same time 5 shares of the common capital stock of the "B" company were issued as qualifying shares to the directors and incorporators of the "B" company who were also directors of the "A" company. The remaining authorized capital stock of the "B" company remained unissued. The fair market value of the said shares of the common

capital stock of the Koster Products Company as of August 28, 1924 did not exceed the sum of \$15.00 a share.

9. This transfer of assets from the "A" company to the "B" company, in exchange for stock of the latter issued to the former, was made to make provision for the payment of debts to certain creditors of the "A" company, aggregating in excess of \$1,000,000.00. These debts arose out of the stockholders liability of the "A" company as a stockholder of the Koster Company, a corporation organized under the laws of the State of California, an insolvent corporation which discontinued its business in 1922. The "A" company upon receipt of said 9,000 shares of the preferred capital stock of the "B" company executed a trust agreement with the Bank of California National Association of San Francisco, as trustee, under date of September 22, 1924, under which it agreed to pay over to said trustee all payments received by it from the "B" company, whether dividends or redemption payments in trust to distribute and pay out the same ratably to the creditors of the "A" company therein listed as beneficiaries of the trust. The "B" company as part consideration for [41] the transfer aforesaid had agreed to assume all of the debts of the "A" company, except those listed and referred to in said trust agreement, the latter being debts arising out of the stockholder liability aforesaid. Following said transfer of assets the "A" company

continued its corporate existence and to pay annual franchise taxes.

10. In November, 1925, the "B" company acquired 50 additional shares of the common capital stock of the Koster Products Company from E. L. Kilbourne, an employee of the "B" company at the time of severing his employment from the "B" company, in settlement of a personal obligation of E. L. Kilbourne to the "B" company.

11. Under date of July 29, 1925, the Supreme Court of California rendered its decision in *Del Monte Light & Power Co. v. Jordan*, 196 Cal. 488. Shortly following said decision, the "B" company tendered to the Secretary of State of the State of California, amended Articles of Incorporation of the "B" company providing that its shares of common capital stock as well as its shares of preferred capital stock should have a par value of \$100.00 per share. The Secretary of State of California acting on the advise of the Attorney General refused to permit the said amended Articles of Incorporation to be filed by the "B" company on the ground that the "B" company was neither a de jure nor de facto corporation. The Secretary of State of California acting on the advice of the Attorney General of the State of California also refused to issue to the "B" company the statutory license to do business in California during the [42] calendar year 1926, when in due time in the month of December, 1925, the prescribed license fee was tendered to him. The license so refused was that required by the provisions

of California Statutes 1915, p. 422 (Chap. 190) as amended Statutes 1917, p. 371, (Chap. 215).

12. In order to meet the foregoing situation the "B" company caused to be incorporated under California laws on December 19, 1925, a corporation under the name of California Barrel Company, Inc. (in the petition and hereinafter referred to as the "C" company). The "C" company is the petitioner herein.

13. Under date of December 10, 1925, the "B" company transferred all of its shares of the capital stock of the Koster Products Company above referred to (8,050 shares) to O. R. Miller and C. L. Koster, for an agreed price of \$8.00 per share (a total consideration of \$64,400.00); payable \$40,000.00 in cash and the balance of \$24,000.00 in promissory notes of \$8,000.00, \$8,000.00, and \$8,400.00, maturing December 21, 1926, December 21, 1927, and December 21, 1928, respectively, with interest at the rate of 6% per annum. The title to the said stock was transferred by delivery of the said stock certificates duly endorsed by the "B" company. The promissory notes of O. R. Miller and C. L. Koster received as part consideration for the stock were made payable to the "B" company, and said promissory notes were duly paid at their respective maturity dates. To the date of said sale no dividends were ever declared or paid by the Koster Products Company on the stock so sold. [43]

14. The Articles of Incorporation of the "C" company authorized the "C" company to engage in

the business of the manufacture and sale of barrels and cooperage. It provided for an authorized capital stock of 18,000 shares divided into 9,000 shares of preferred capital stock, and 9,000 shares of common capital stock, both of a par value of \$100.00 a share and both having voting rights. It provided for the same preferences for its preferred shares as were provided for the preferred shares of capital stock of the "B" company.

15. The "B" company by a deed of conveyance dated December 29, 1925, transferred as of December 31, 1925, to the "C" company all of its assets in consideration for capital stock issued as follows:

9,000 shares of preferred capital stock to "A" company.

125 shares of common capital stock to Frederick J. Koster.

125 shares of common capital stock to B. J. Critcher, as Trustee for the stockholders of "A" company other than Frederick J. Koster, in proportion to their stockholdings in the "A" company.

The said deed of conveyance was executed by the "B" company as first party and grantor and the "A" company as second party and by the "C" company as third party and grantee. As further consideration for this transfer, the "C" company agreed to assume all of the liabilities of the "B" company. At the same time 5 qualifying shares of the common stock of the "C" company were issued

to its five incorporators and directors. The remaining shares of common stock of the "C" company remained unissued. No steps have been taken to dissolve the "B" company and no decree of court dissolving the same has even been entered. [44]

16. The "A" company upon receipt of 9,000 shares of the preferred capital stock of the "C" company executed a Trust Agreement with the Bank of California National Association of San Francisco, as Trustee, under date of February 26, 1926, under which it agreed to pay over to said Trustee all payments received by it from the "C" company as dividends or redemption payments in trust, to pay out the same ratably to the creditors of the "A" company therein listed as beneficiaries of the trust, which list was a duplicate of the list of beneficiaries in the former trust agreement with said bank of September 22, 1924, hereinabove referred to. The "A" company after receiving the 9,000 shares of the preferred capital stock of the "C" company as aforesaid, continued to hold the same until September 30, 1926, at which time through the retirement of 270 shares of said preferred stock, its holdings were reduced by that amount. Except for the retirement of said 270 shares, no change since September 30, 1926, has occurred in the "A" company's ownership of the "C" company's preferred capital stock.

17. Immediately prior to the said transfer of assets from the "B" company to the "C" company

the officers, directors, and stockholders of the "B" company were as follows:

Officers

Frederick J. Koster, President; S. P. White, Secretary; Wm. B. Duff, Vice-President; John A. Koster, Treasurer; H. F. Marten, Supt. San Francisco Branch; J. J. Krohn, Manager Arcata Branch.

Directors

Frederick J. Koster, Willard J. Growall, John A. Koster, William B. Duff, J. J. Krohn. [45]

Stockholders

"A" company—9,000 shares preferred stock. The aforesaid directors of the "B" company who were also the five directors and stockholders of the "A" company—1 share of common stock each. Frederick J. Koster, a stockholder of "A" company—505 shares of common stock. B. J. Critcher, Trustee, who held the stock as Trustee under a Trust Agreement between her and F. J. Koster for the stockholders of the "A" company other than Frederick J. Koster, in proportion to their stockholdings in "A" company—490 shares common stock.

18. Immediately following the said transfer of the assets by the "B" company to the "C" company, the officers, directors, and stockholders of the "C" company were as follows:

Officers

Frederick J. Koster, President; S. P. White, Secretary; Wm. B. Duff, Vice-President; John A.

Koster, Treasurer; H. F. Marten, Supt. San Francisco Branch; J. J. Krohn, Manager Arcata Branch.

Directors.

Frderick J. Koster, Willard L. Growall, John A. Koster, William B. Duff, Shelley P. White (later, March 25, 1926, succeeded by J. J. Krohn).

Stockholders

“A” company—9,000 shares preferred stock. Five directors of “C” company who were also directors and stockholders of the “B” company—1 share of common stock each,—5 shares common. Frederick J. Koster, a stockholder of “A” and “B” companies—125 shares common—B. J. Critcher, Trustee, who held the stock as a Trustee under a Declaration of Trust made by her for the stockholders of “A” company other than F. J. Koster, in proportion to their stockholdings in the “A” company—125 shares common.

19. The term of existence of the “B” company as provided in its Articles of Incorporation was 50 years from February 15, 1924, and the term of existence of the “C” company was 50 years from December 19, 1925.

20. For Federal income tax purposes, timely corporation income tax returns were filed for the calendar years 1924, 1925, 1926, and 1927 as follows, copies of which are hereto attached as Exhibits 2, 3, 4, 5, 6 and 7, respectively, all of which are made a part hereof:

1924—“B” company separate return—Exhibit 2

1925—“A” company separate return—Exhibit 3

1925—"B" company separate return—Exhibit 4

1925—"C" company separate return—Exhibit 5

1926—"A" company, "C" company consolidated
return—Exhibit 6

"B" company, no return

1927—"A" company, "C" company consolidated
return—Exhibit 7

"B" company, no return.

Nothing in this paragraph shall be deemed an admission by either party for the purposes of this appeal of the correctness of the returns so filed.

21. For Federal income tax purposes the "A" company and the "C" company filed consolidated corporation income tax returns for the calendar years 1926 and 1927, but neither of the companies did apply for, or receive from the Commissioner of Internal Revenue formal permission to file a consolidated income tax return for the calendar year 1926 or 1927.

22. As shown in the corporation income tax return of the "B" company for the calendar year 1925, a loss was claimed by said company on the sale of the capital stock of the Koster Products Company in the amount of \$846,461.85. As shown on the consolidated return of the "A" company and the "C" company, for the calendar year 1927, a statutory net loss was claimed by the petitioner ("C" company) in the amount of \$306,348.56 as a portion of the alleged loss shown on the [47] corporation income tax return of the "B" company for the calendar year 1925.

23. In the computation of taxable net income of the "C" company for the calendar year 1927 the Commissioner of Internal Revenue in his deficiency letter dated December 12, 1929, a copy of which is attached to the petition, and incorporated herein by reference, disallowed the amount of the said statutory net loss claimed by the "C" company as a deduction.

This appeal was filed with the Board of Tax Appeals with respect to respondent's disallowance of said statutory net loss.

DATED: September 14, 1933.

ALLEN G. WRIGHT

T. H. LAWRENCE

Counsel for Petitioner

E. BARRETT PRETTYMAN

General Counsel—Bureau of Internal Revenue
—Counsel for Respondent. [48]

EXHIBIT 1

United States Board of Tax Appeals

Docket No. 47419

CALIFORNIA BARREL COMPANY, INC.

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

STATEMENT SHOWING COST OF TIMBER-
LANDS SITUATE IN THE STATE OF

OREGON, AND IN THE STATE OF WASHINGTON TOGETHER WITH IMPROVEMENTS THEREON AND OTHER ASSETS WHICH WERE TRANSFERRED TO THE KOSTER PRODUCTS COMPANY ON MAY 31, 1919

Cost of Oregon timberlands	\$353,853.66	
Cost of Washington timberlands, acquired during 1918	28,573.00	\$382,426.66
	<hr/>	
Less depletion on timberlands to May 31, 1919		26,160.11
		<hr/>
Cost of timberlands, less depletion to May 31, 1919,		\$353,266.55
Cost of railroad, logging equipment, etc.:		
Current assets		92,258.27
Railroad, logging equipment, etc.	\$444,158.13	
Less depreciation to May 31, 1919	43,023.16	
	<hr/>	
Cost of other plant assets, less depreciation to May 31, 1919	\$401,134.97	
Less plant liabilities	108,285.58	
	<hr/>	
Net cost of plant		\$292,849.39
		<hr/>

Total cost of all assets exclusive of carrying charges noted below less depletion and depreciation to May 31, 1919	\$738,374.21
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In addition to the above costs the "A" company paid carrying charges consisting of interest, taxes, insurance, etc., from the date of the acquisition of the above described timberlands to May 31, 1919, as follows:

Carrying charges to 1910	\$ 56,904.00
Carrying charges years ended June 30, 1911, 1912, and 1913:	
Interest	\$ 62,274.94
Taxes	3,701.97
Other	17,453.69
	83,430.60
Carrying charges subsequent to 1913	29,493.04
Total	\$169,827.64

[49]

I hereby certify that the foregoing is a true and correct statement of all the evidence adduced at the hearing before the United States Board of Tax Appeals which, with the exhibit hereto attached and those to be sent to the Court under its order, is ma-

terial to the assignments of error set out in the petition for review.

(Signed) GEO. E. H. GOODNER
Counsel for Petitioner.

I have no objection to the foregoing statement of evidence and the accompanying exhibit.

ROBERT H. JACKSON
Assistant General Counsel for the Bureau of
Internal Revenue. Counsel for Respondent.

Settled and approved this 26th day of February,
1935.

(s) J. RUSSELL LEECH
Member, United States Board of Tax Appeals.

[Endorsed]: Filed Feb. 26, 1935 [50]

[Title of Court and Cause.]

PRAECIPE FOR RECORD

TO THE CLERK OF THE UNITED STATES
BOARD OF TAX APPEALS:

You are hereby requested to prepare and certify and transmit to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, with reference to petition for review heretofore filed by the petitioner in the above cause, a transcript of record in the above cause, prepared, certified and transmitted as required by law and by the rules of said Court, and to include in said transcript

of record the following documents or certified copies thereto, to-wit:

(1) The docket entries of all proceedings before the Board of Tax Appeals.

(2) Pleadings before the Board of Tax Appeals as follows:

(a) Petition for redetermination.

(b) Answer of respondent. [51]

(3) The memorandum opinion of the Board.

(4) The decision of the Board.

(5) The petition for review, filed by the petitioner in the above cause.

(6) Notice of filing petition for review.

(7) The statement of the evidence including the Stipulation of Facts and Exhibit 1 attached.

(8) This praecipe.

Will you also please forward to the Clerk of the Court, pursuant to the Court's order entered on or about February 19, 1935, the following original exhibits filed in this case at the hearing, viz.:

Exhibit 2—1924 Income Tax Return

(“B” company)

Exhibit 3—1925 Income Tax Return

(“A” company)

Exhibit 4—1925 Income Tax Return

(“B” company)

Exhibit 5—1925 Income Tax Return

(“C” company)

Exhibit 6—1926 Income Tax Return

(“A” and “C” company consolidated)

Exhibit 7—1927 Income Tax Return

(“A” and “C” company consolidated)

ALLEN G. WRIGHT

RANDELL LARSON

Attorneys for Petitioner

1012 Mills Building

San Francisco, California.

[Endorsed]: Filed Feb. 26, 1935. [52]

[Title of Court and Cause.]

CERTIFICATE

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages, 1 to 52, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 1st day of April, 1935.

[Seal]

B. D. GAMBLE

Clerk, United States Board of Tax Appeals.

[Endorsed]: No. 7826. United States Circuit Court of Appeals for the Ninth Circuit. California Barrel Company, Inc., Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Upon Petition to Review an Order of the United States Board of Tax Appeals.

Filed April 8, 1935.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of
Appeals for the Ninth Circuit.

7
No. 7826

IN THE
United States Circuit Court of Appeals
For the Ninth Circuit

CALIFORNIA BARREL COMPANY, INC.,
Petitioner,

VS.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

BRIEF FOR PETITIONER.

Upon Petition to Review an Order of the United States
Board of Tax Appeals.

ALLEN G. WRIGHT,
RANDELL LARSON,
Mills Building, San Francisco,
Counsel for Petitioner.

FILED

OCT 5 - 1935

PAUL P. O'BRIEN,

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No. 7826

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

CALIFORNIA BARREL COMPANY, INC.,
Petitioner,

VS.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

BRIEF FOR PETITIONER.

Upon Petition to Review an Order of the United States
Board of Tax Appeals.

I.

ABSTRACT OF THE CASE.

1. PRELIMINARY STATEMENT.

The B company organized in February, 1924, and the C company (the taxpayer and petitioner herein) organized in December, 1925, both were California corporations engaged in the manufacture and sale of barrels and cooperage (Trans. p. 41, par. 7, p. 45, pars. 12, 14) owned and controlled by the same stockholders with like officers and directors (Trans. pp. 47, 48, 49, pars. 17, 18).

The B company in its income tax return for the calendar year 1925, claimed a loss of \$846,461.85 (Ex.

4, Schedule B, on file herein) which, when a part of it was applied against income, left a statutory net loss of \$504,502.66 which, under authority of Sec. 206(b) of the Revenue Act of 1926, it would have been entitled to deduct from its 1926 income and if not extinguished by that deduction it would have been entitled, under the same act, to deduct the remaining statutory net loss from its 1927 income.

The B company transferred all its assets and business to the C company as of December 31, 1925, in exchange for the redeemable preferred stock and the common stock of the C company (Trans. p. 46, par. 15). The preferred stock of the C company in the same principal amount as that theretofore issued by the B company went to the A company as B company's nominee (Trans. p. 46, par. 15, pp. 47, 48, 49, pars. 17, 18). The common stock of the C company went to the common stockholders of the B company as the latter's nominee (Trans. p. 46, par. 15, pp. 47, 48, 49, pars. 17, 18). The C company had been organized in December, 1925, to take over the assets and the business of the B company *under exceptional circumstances* to avoid any threatened discontinuance of the enterprise in which the B company had been engaged and which the C company thereafter continued (Trans. pp. 44, 45, pars. 11, 12). In its income tax returns for 1926 and 1927 the C company had claimed as the *alter ego* of the B company a statutory net loss representing the unextinguished net statutory loss asserted by the B company in its 1925 return. The return of the C company for 1926 was not questioned by the Commissioner and is not involved in the present proceeding.

The respondent, however, advised the petitioner, the C company, that the statutory net loss claimed by the C company for 1927 could not be allowed and asserted a deficiency in tax liability accordingly of \$14,915.65. The reason assigned for this decision was that the B company and the C company were different taxable entities (Trans. pp. 9 to 16). From this decision the petitioner appealed to the Board of Tax Appeals for a redetermination of the asserted tax liability. After the case was submitted to the Board early in January, 1934 (Trans. p. 3), but before the Board rendered its decision in November, 1934, the Supreme Court rendered its opinion May 28, 1934, in *New Colonial Ice Co., Inc. v. Helvering*, 292 U. S. 435. The Board of Tax Appeals in deciding the present case said:

“The facts and contentions here involved are similar to those in *New Colonial Ice Co., Inc. v. Helvering*, 292 U. S. 435. * * * Upon authority of *New Colonial Ice Co., Inc.*, supra, we hold that petitioner, the ‘C’ company, is not entitled to a deduction in 1927 for any portion of a net loss sustained in 1925 by its predecessor the ‘B’ company. This conclusion obviates the necessity of determining the correct amount of the alleged net loss sustained by ‘B’ company” (Trans. pp. 22, 23).

The Board accordingly assessed a deficiency tax against the petitioner in the sum of \$14,915.65 (Trans. p. 24).

In assuming that the facts and contentions in this case were similar to those involved in the *New Colonial Ice Co.* case, the Board, it is suggested, was in error.

In the *New Colonial Ice Co.* case, the court announced that, as a general rule two corporations, though the stockholders of the two were substantially the same, for tax purposes would be regarded as separate entities but that this general rule was "subject to the qualification that the separate entity might be disregarded in exceptional situations where it otherwise would present an obstacle to the due protection or enforcement of public or private rights". The petitioner suggests that such an exceptional situation is present in this case, as will be later developed herein, and that because the separate entity may be disregarded by reason of such an exceptional situation the petitioner and the B company may be recognized as the same taxpayer within the meaning of Sec. 206(b) of the Revenue Act of 1926. After the Board rendered its decision, this court in January, 1935, rendered its decision in *McLaughlin v. Purity Inv. Co.*, 75 Fed. (2d) 30, rehearing denied March 25, 1935, in which, on the authority of the *New Colonial Ice Co.* case, it refused to recognize two corporations as the same taxpayer within the meaning of Sec. 206(b) of the Revenue Act of 1926. The petitioner also suggests, for reasons which will be presently submitted herein, that its case is distinguishable on the facts from the *Purity Inv. Co.* case.

This case was tried below on an agreed statement of facts (Trans. pp. 38 to 53) and on Exhibits 1, 2, 3, 4, 5, 6 and 7 attached thereto. Exhibit 1 is set forth in the Transcript pp. 51, 52, 53. The original Exhibits 2, 3, 4, 5, 6 and 7 pursuant to an order of this court have been forwarded to and filed with the clerk of this

court. These original exhibits so filed herein are the income tax returns of the corporations concerned for the years 1924, 1925, 1926 and 1927.

2. FEDERAL STATUTES INVOLVED.

Sec. 206(b) of the Revenue Act of 1926 (26 U. S. C. A. Sec. 937(b), Sec. 206, 44 Stat. 17) reads as follows:

“If, for any taxable year, it appears upon the production of evidence satisfactory to the commissioner that any taxpayer has sustained a net loss, the amount thereof shall be allowed as a deduction in computing the net income of the taxpayer for the succeeding taxable year (hereinafter in this section called ‘second year’) and if such net loss is in excess of such net income (computed without such deduction), the amount of such excess shall be allowed as a deduction in computing the net income for the next succeeding taxable year (hereinafter in this section called ‘third year’); the deduction in all cases to be made under regulations prescribed by the commissioner with the approval of the Secretary.”

Extracts from other Revenue Acts incidentally involved are set forth in Appendix “A” to this brief.

3. QUESTIONS INVOLVED.

The questions raised here are questions of law.

(1) This case raises the right of the C company, under the special circumstances of this case, to deduct

from its 1927 income an unextinguished statutory net loss arising from a net loss sustained by its predecessor the B company in 1925. One question here, therefore, is whether the petitioner by reason of an exceptional situation in its case, which will be later disclosed, comes within the exception noted in the *New Colonial Ice Co.* case and whether, therefore, the practical identity of the B company and the C company may be acknowledged and both recognized to be the same taxpayer, within the meaning of Sec. 206(b) of the Revenue Act of 1926.

(2) Another question is whether this case on its facts is so distinguishable from the *Purity Inc. Co.* case that the decision in that case is not controlling here.

(3) Finally, a question is presented which concerns the time when the loss originally asserted by the B company and carried over as a statutory net loss by the C company was actually realized so as to form the basis for taxable gain or loss within the purview of the Revenue Acts. The determination of the time of this loss will also settle the amount of this loss, all the facts of the case being agreed upon.

II.

SPECIFICATION OF ERRORS TO BE RELIED UPON.

(1) The Board erred in making and entering its decision in this cause and in entering judgment in favor of the Commissioner and against the taxpayer.

(2) The Board erred in its conclusions of law and its application of the law to the facts.

(3) The Board erred in that the opinion, decision and order of the Board are contrary to the evidence and are not supported by the evidence.

(4) The Board erred in that the opinion, decision and order of the Board are contrary to the facts stipulated in this case and are not supported by the facts stipulated in this case.

(5) The Board erred in determining a deficiency against this taxpayer for the year 1927 amounting to \$14,915.65.

(6) The Board erred in holding that the taxpayer hereinabove referred to as the 'C' company was not entitled to a deduction in 1927 for any portion of a net loss sustained in 1925 by its predecessor hereinabove referred to as the B company.

(7) The Board erred in finding that the two corporations hereinabove referred to respectively as the B company and the C company were in fact distinct corporations.

(8) The Board erred in concluding that the said B company and C company were in law distinct corporations.

(9) The Board erred in concluding that the said B company and C company were not one and the same taxpayer.

(10) The Board erred in failing to find or conclude that there is no income tax due from the taxpayer for 1927.

(11) The Board erred in not accepting and stating as its findings of fact all the facts stipulated in this case as the basis for its said opinion, decision and order.

(12) The Board erred in that the opinion and decision of the Board, based upon the facts stipulated in this case, are contrary to law.

III.

ARGUMENT.

1. THE EXCEPTIONAL CIRCUMSTANCES OF THIS CASE.

The petitioner has suggested that there are exceptional circumstances in this case which bring it within the exception to the general rule announced and applied in the *New Colonial Ice Co.* case and has also suggested that the circumstances of this case differentiate it from the *Purity Inv. Co.* case. These circumstances will now be developed.

The B company caused the C company to be incorporated to meet a situation (Trans. p. 45, par. 12) brought about by the wrongful conduct of the California Secretary of State which threatened the continuous operation of the business enterprise of the B company. The organization of the C company and the transfer of its assets and business by the B company to the C company were not deliberate and voluntary acts in the same sense that the creation of a new company and the transfer to it of the assets of the old company in the *New Colonial Ice Co.* case were deliberate and voluntary acts.

The circumstances under which the C company was organized and the transfer was made by the B company to the C company were as follows:

The B company filed its articles of incorporation with the California Secretary of State February 15, 1924, who thereupon issued his certificate of the incorporation thereof (Trans. p. 41, par. 7). Its articles provided that its capital stock should consist of 18,000 shares divided into 9000 shares of redeemable preferred stock with a par value of \$100.00 per share and 9000 shares of common stock with no par value, both having voting rights (Trans. p. 41, par. 7). A corporation might then be organized in California according to the literal terms of the statutory law with two classes of stock, one with and the other without a par value (Civil Code Secs. 290b, 290c, 290d, 290e and 290f, as amended California Stats. 1923, p. 621, Chap. 293, set forth in Appendix "B" to this brief).

Under date of July 29, 1925 (rehearing later denied), the Supreme Court of California rendered its decision in *Del Monte Light & Power Co. v. Jordan*, 196 Cal. 488. That case was a mandamus proceeding against the Secretary of State to secure a writ directing him to file certain amended articles of incorporation of the plaintiff. The plaintiff, it appeared, was a California corporation organized in 1919 with a capital stock divided into preferred and common shares, both having the same par value. The plaintiff in said proceeding, it appeared, acting under authority of the aforesaid provisions

of the Civil Code so added thereto in 1923, proceeded in August, 1924, to amend its articles of incorporation so as to provide for a capital stock divided into preferred and common shares, the preferred shares to have a par value, and the common shares to have no nominal or par value. When these amended articles of incorporation were presented to the Secretary of State for filing in his office—a step necessary to make them effective (California Civil Code Sec. 362, as amended 1921, Stats. 1921, p. 134, Chap. 134, set forth in Appendix “B” to this brief)—the Secretary of State refused to permit their filing in his office, and the application for a writ of mandate against him then followed. The court, in that case, denied the writ, holding that the sections so added to the Civil Code in 1923 were in violation of certain provisions of the California Constitution, to-wit, Secs. 3 and 12 of Article XII thereof. These sections referred to the voting rights of stockholders in a corporation and their proportional liability as stockholders for the debts and liabilities of the corporation. The decision determined that the provisions of these sections required that the capitalization of corporations, to give effect thereto, should be represented in shares of a single par value.

In 1925 and in 1926, by virtue of the provisions of certain California statutes (Calif. Stats. 1915, p. 422, Chap. 190, as amended Calif. Stats. 1917, p. 371, Chap. 215, excerpts from which are set forth in Appendix “C” to this brief) every corporation doing

an intrastate business in the State of California, with certain exceptions not pertinent to the instant case, was obliged to procure annually from the Secretary of State, a license authorizing the transaction of such business in the State and was obliged to pay the prescribed license tax therefor. This tax was graded according to the authorized capital stock of the company concerned and was due and payable on the first day of January of each year (Sec. 3). Notice of the tax for the succeeding calendar year was to be mailed by the Secretary of State to every corporation concerned on or before December first of each year (Sec. 9). Failure to pay the tax made the corporate rights, privileges and powers of a domestic corporation suspended and incapable of being exercised (Sec. 11). When the rights, privileges and powers of the corporation were so suspended every person who attempted or purported to exercise any of the rights, privileges or powers of such a corporation was guilty of a misdemeanor and punishable by substantial fine or by imprisonment or by both and every contract made in violation of the statute, the statute itself expressly made void (Sec. 11).

Following the decision of the California Supreme Court in *Del Monte Light & Power Company v. Jordan*, supra, the B company tendered to the Secretary of State of the State of California, its amended articles of incorporation, providing that its shares of common stock, as well as its shares of preferred stock, should have a par value of \$100.00 per share (Trans. p. 44, par. 11). The Secretary of State, acting

on the advice of the Attorney General, refused to permit the B company to file said amended articles of incorporation, on the ground that the B company was neither a *de jure* nor a *de facto* corporation (Trans. p. 44, par. 11). The Secretary of State, acting on the advice of the Attorney General, also refused to issue to the B company the statutory license to do business in California, during the year 1926, required by said statutes of 1915 and 1917, when in due time in the month of December, 1925, the prescribed license fee was tendered to him (Trans. p. 44, par. 11).

It was to meet the foregoing situation that the B company caused the C company to be incorporated on December 19, 1925, as aforesaid (Trans. p. 45, par. 12), and transferred its assets to the C company as of December 31, 1925 (Trans. p. 46, par. 15).

The circumstances of the B company at this juncture were such that it could not risk any actual or threatened interference with its continued business operations. To understand those circumstances fully it is necessary first to go back to the organization of the B company.

The B company had been organized in 1924 by the directors of the A company as its incorporators (Trans. p. 42, par. 8). The A company, a California corporation, had been organized in 1906 to engage in the manufacture and sale of barrels and cooperage (Trans. p. 39, par. 2). On August 28, 1924, with the authority of its directors, stockholders and all its creditors, the A company transferred all its business

and properties to the B company in exchange for 9000 shares of its preferred capital stock, par value \$100.00 per share, and 995 shares of its common no par value stock which went to the stockholders of the A company as its nominees (Trans. p. 42, par. 8). This transfer of assets from the A company to the B company in exchange for stock was made to make provision for the payment of debts to certain creditors of the A company aggregating in excess of \$1,000,000.00. These debts arose out of the stockholders' liability of the A company as a stockholder of an insolvent California corporation which had discontinued its business in 1922 (Trans. p. 43, par. 9). The preferred shares of the B company thus received by the A company were redeemable shares carrying accumulated dividends at specified rates supported by a sinking fund (Trans. p. 41, par. 7). The A company under the terms of a trust agreement made by it with The Bank of California National Association as Trustee, agreed to pay over to the Trustee all payments received by it from the B company whether dividends or redemption payments such Trustee to pay out the same ratably to the creditors of the A company therein listed as beneficiaries of the trust. So far as the preferred stock of the B company was concerned, A company was in effect a holding company. The common stock of the B company was owned by the stockholders of the A company. The A company and the B company were controlled and owned by the same group of individuals and they all had a common interest in keeping faith with the creditors of

the A company who had been provided for by this trust agreement.

In addition the business interests, the investments, and the financial obligations of the B company were substantial. The B company in its income tax return for 1925 (Ex. 4), disclosed an inventory at the beginning of the year of \$370,239.72, an inventory at the close of the year of \$407,422.97, with total assets of \$1,582,714.34, including machinery and equipment of \$407,744.29, and a bonded debt of \$194,000.00 and a mortgage debt of \$1800.00, and notes and accounts payable amounting to \$173,659.05.

The possible effect of the decision in the *Del Monte Light & Power Co.* case on the corporate character of the B company concerned not only the creditors of the A company who had to look to the B company for any realization on its preferred stock, but it also concerned the direct creditors of the B company, as well as the stockholders of that company and its future business enterprise. If the B company had been so wedded to a capital stock structure with par value preferred shares and non par value common shares that it could suffer no divorce therefrom, it might have solved the dilemma as the *Purity Inv. Co.* did, by organizing a new corporation under the Nevada law with such a stock structure. The first reaction of the B company to the decision in the *Del Monte Light & Power Co.* case was not to invoke the law of another jurisdiction but was to make an effort to put its own house in order and through an amendment of its articles of incorporation to change its

capitalization to one represented by shares of a single par value and thus to harmonize its capitalization with the provisions of the California Constitution.

Such amended articles of incorporation the Secretary of State refused to permit the B company to file in his office on the grounds that the B company was neither a *de jure* nor a *de facto* corporation. Until filed in his office these amended articles of incorporation were without effect (California Civil Code 362 as amended 1921, *supra*). The Secretary of State, however, should have permitted the B company to file these amended articles of incorporation. Later, in a decision rendered May 19, 1926 (rehearing later denied), in *Westlake Park Investment Co. v. Jordan*, 198 Cal. 609, 618, the court held that the plaintiff in that case, a California corporation organized in 1925 with a capitalization like that of the B company represented by preferred shares with a par value and by common shares with no par value, was nevertheless a *de facto* corporation and as such entitled to amend its articles of incorporation and to file them in the office of the Secretary of State as so amended. Had the Secretary of State, in the latter part of 1925, not been misguided as to the law when the B company presented its amended articles of incorporation for filing in his office, and had he filed the same the problem of the B company would have been solved. By so amending its articles of incorporation as it attempted to do, the B company would have cured the irregularity in its original incorporation and have acquired a capitalization

harmonious with the provisions of the California Constitution. There would then have been no necessity for organizing the C company.

Following this refusal of its amended articles of incorporation the B company in December, 1925, tendered its license fees for 1926 and requested the statutory license to do business in California in 1926. The fees were refused and the license denied by the Secretary of State on the grounds and under the advice of the Attorney General already referred to (Trans. p. 44, par. 11). The Secretary of State had no right to refuse these fees or to deny this license as was subsequently determined in the *Westlake Park Investment Co.* case, *supra*. The penalties to which the B company and its officers would be exposed if it attempted to transact business in 1926 without paying its license fees and securing a license have been noted above. Not only would its officers and employees be liable to criminal prosecution but its contracts made in 1926 would be void. The business, the investment, and the financial obligations of the B company were too substantial to be thus left in jeopardy. To continue the business in 1926 it was essential that the B company should be free to exercise its rights, privileges and powers as a corporation and should be free to make, perform and enforce contracts without risk of penalty to itself or its officers or employees, and without having the validity of its contracts open to question. But there was no such court decision as that in the *Westlake Park Investment Co.* case to govern the situation as the year 1925 approached its close. The B company had done

what it could to avoid the creation of the C company. It had amended its articles of incorporation to conform its capital stock structure to the standards insisted upon by the court in the *Del Monte Light & Power Company* case, but it had not been allowed to file them so as to make these amended articles effective. It had requested a statutory license to do business in 1926 and tendered the prescribed fee therefor in due time and had been denied the license. The B company desired to avoid a disruption of its business from and after January 1, 1926. It wished to avoid the expense, delay, and uncertainty of possible litigation over its future contracts. It wanted to avoid placing itself and its officers and employees in possible jeopardy of the penalties prescribed by the licensing statutes of the state. It sought a way to continue with its business enterprise. It felt obliged to protect the interests of its stockholders and its creditors. It was anxious to conserve its property interests. In order to act in good faith toward all concerned with its enterprise it was not only necessary but imperative for it to take some immediate action. Accordingly, it provided for the creation of the C company and the transfer of its assets to the C company as of December 31, 1925. That course, we think, must be evident as the only safe, certain and prompt solution of the problem with which it was confronted. The time elements did not permit any other course. That the C company was created to meet this situation arising from the *Del Monte Light & Power Company* decision and the refusal of the Secretary of State to permit the B company to amend its articles

of incorporation, as aforesaid, and his denial of a statutory license to the B company for 1926 is not only stipulated herein (Trans. pp. 44, 45) but that the creation of the C company and the transfer to it of the assets of the B company had no other motive, is, we suggest, further evident from the substantial identity of the B company and the C company in all essential matters. The C company, except that in form it was a new entity, was in no essential different from what the B company would have been if the latter had been permitted in 1925 to file its amended articles of incorporation.

The C company, like the B company, issued nine thousand (9,000) shares of preferred stock to the A company (Trans. p. 42, par. 8, pp. 46, 47, par. 15). The A company upon receipt of these nine thousand (9,000) shares of the preferred stock from the C company executed with respect to them a trust agreement with The Bank of California National Association of San Francisco, as Trustee, similar to the trust agreement of which the preferred shares of the B company were the subject (Trans. pp. 41, 42, par. 7, pp. 45, 46, par. 14). The ultimate beneficial interest in the nine thousand (9,000) preferred shares of the B company was the same in the nine thousand (9,000) preferred shares of the C company. Both sets of shares had the same par value and the same preferences (Trans. pp. 41, 42, par. 7, pp. 45, 46, par. 14).

The preferred shares and the common shares of the B company and the C company, both had voting rights (Trans. pp. 41, 42, par. 7, pp. 45, 46, par. 14).

The C company operated under the same management as the B company (Trans. pp. 47, 48, par. 17, pp. 48, 49, par. 18).

The stock of the two companies immediately before and immediately after the transfer of the assets of the B company to the C company, effective December 31, 1925, was held as stated below (Trans. pp. 47, 48, par. 17, pp. 48, 49, par. 18). All of the stock of the B company was held by the A company or its stockholders directly or through B. J. Critcher, trustee, and all of the stock of the C company was held by the A company or its stockholders directly or through B. J. Critcher, Trustee, except that one qualifying director's share in the C company was held only temporarily by White, and later taken over by Krohn, a stockholder of the A company. Further the stock of the B company and the stock of the C company was not only thus owned by the same interests, but the capital stock liability of both was substantially the same, as appears from a comparison of Ex. 4 with Ex. 6, after allowing for preferred stock redeemed September 30, 1926, in the sum of \$27,000.00 (Trans. p. 47, par. 16). The total capital stock liability of the B company and C company at the beginning of 1926, and before any redemption of preferred stock varied therefore by only \$125.00, due probably to the fact that B company common stock had no nominal or par value, while C company common stock had a par value of \$100.00 per share, and an effort was made to avoid fractional shares.

The A company owned the total authorized preferred stock of the B company and also of the C company, that is nine thousand (9,000) shares in each. Those ultimately beneficially interested in the preferred stock of the B company and in the preferred stock of the C company under the trust agreements referred to are the same, as already noted. Frederick J. Koster owned 50.6 per cent of the common stock of the B company and 49.41 per cent of the common stock of the C company. B. J. Critcher, Trustee, owned 49 per cent of the common stock of the B company and 49.02 per cent of the common stock of the C company. The A company owned 97.24 per cent of the voting stock of the C company until September 30, 1926, when with the retirement of 270 shares of preferred stock it held 97.16 per cent of the voting stock of the C company, which it continued to hold through 1926 and 1927 (Trans. p. 47, par. 16). Expressed in dollar values the common shares of the B company and the C company would be reflected as follows:

Stockholder	B company shares	C company shares
Frederick J. Koster	\$12,939.75	\$12,600.00
B. J. Critcher, Trustee	12,433.75	12,500.00
Four directors other than Frederick J. Koster	101.50	400.00
	<hr/> \$25,375.00	<hr/> \$25,500.00

As the directors of California corporations in 1925, 1926 and 1927, must have been stockholders (Calif. Civil Code Sec. 305, as amended 1905, Stats. 1905 p.

503, chap. 305, set forth in Appendix "B" to this brief) the foregoing distribution was as substantially identical on a valuation basis in the holdings of common stock in the B company and the C company, as was practically possible, if fractional shares were to be avoided, with a stock having a par value of \$100.00 per share.

The C company continued the business of the B company with the property taken over from the B company, as is reflected in the income tax returns (consolidated) of the A company and the C company for 1926 and 1927 (Exs. 6 and 7), when compared with the income tax return of the B company for 1925 (Ex. 4).

Every effort was therefore made to make the C company and the interests therein as like as possible to the B company and the interests therein, and it must be apparent therefore that the only motive in organizing the C company was that motive which has been stipulated herein, namely, to meet the situation created by the unlawful conduct of the Secretary of State in refusing to file the offered amended articles of incorporation of the B company and in denying the latter a license for 1926.

2. THE DISTINCTION BETWEEN THIS CASE AND THE PURITY INV. CO. CASE.

In the *New Colonial Ice Co.* case the bare bones of the case was one where the old company freely and voluntarily organized a new company and transferred

to it the assets of the old company for stock in the new which became the property of the stockholders of the new company in substantially like proportions to their holdings in the old company. For purposes of claiming a statutory net loss in 1922 and 1923 the new company based its claim on a net loss suffered by the old company in 1921. The court held that the new company was not the taxpayer who had suffered the loss and was therefore not entitled to claim the statutory net loss in 1922 and 1923 under Sec. 204(b) of the Revenue Act of 1921. In the course of its opinion the court commented on the fact that "the transaction was voluntary and contractual and not by operation of law". In the supporting cases cited by the court in that decision and in the cases referred to therein with comments of disapproval the transactions were all voluntary. The same may be said of the cases which we have examined which have since cited and followed the decision in the *New Colonial Ice Co.* case. In none of them have we found a case where the new organization was not the result of free and voluntary action unaffected by such forces of compulsion as existed in the case at bar unless it be the *Purity Inv. Co.* case. That case, however, upon analysis, reveals that the formation of the new corporation there was the result of voluntary action on the part of those concerned with free opportunity of a choice and that the motive of the organizers was not to preserve the identity of the old company but was very frankly to bring forth a new and distinct entity. This court, therefore, properly declined to distinguish

the *Purity Inv. Co.* case from the *New Colonial Ice Co.* case.

The following circumstances distinguish the *Purity Inv. Co.* case from the case at bar and emphasize the point which the petitioner desires to make in its case.

The Purity Inv. Co. of Nevada was the holding company of the Purity Stores, Inc. of Nevada. The Purity Stores, Inc. of California was incorporated February 26, 1925, with a capital stock represented by preferred stock having a par value and common stock having non par value. It had secured permission from the Corporation Commissioner to issue its stock on March 17, 1925. Four months later, on July 29, 1925, the decision was rendered in the *Del Monte Light & Power Co.* case which, however, did not become final until thirty days later when rehearing was denied. Thereupon the Corporation Commissioner denied the Purity Stores, Inc. the authority to issue further stock. How much stock had been issued in the five months following the original authority of the Corporation Commissioner does not appear, but evidently not all which the original permit authorized. Whether the Purity Stores, Inc. ever tendered or paid to the Secretary of State its license fees for 1926 is not disclosed by the opinion, though reference is made to the Secretary's opinion that such corporations as the Purity Stores, Inc. were not *de facto* corporations and were not entitled to a license authorizing them to transact business. Apparently, however, the Purity Stores, Inc. continued to do business until December 31, 1926, when all of its assets were transferred to the

Purity Stores, Inc. of Nevada, incorporated there on December 27, 1926. After being denied authority to issue more stock by the Corporation Commissioner some time in the latter half of 1925, the California corporation continued to receive money on stock subscriptions and issued interim certificates therefor. The Purity Stores, Inc. of California did not, like the B company, make an attempt to amend its articles of incorporation to change its stock structure so as to harmonize it with the provisions of the California Constitution as interpreted in the *Del Monte Light & Power Co.* case. Following the decision in the *Westlake Park Investment Co.* case on May 19, 1926, rehearing denied thirty days later, the Secretary of State on June 22, 1926, addressed a letter to the Purity Stores, Inc. advising that under the decision in the *Westlake Park Investment Co.* case it was a *de facto* corporation and entitled to enjoy the privileges of a corporation until an action for dissolution was brought by the Attorney General pursuant to Sec. 358 of the Civil Code. The Purity Stores, Inc. of California must have known of its right to amend its articles of incorporation under authority of the decision to which its attention was thus directed, and thereby conform its stock structure to constitutional requirements and acquire a *de jure* character free from the threat of *quo warranto* proceedings. Such an amendment would have paved the road to a new permit from the Commissioner of Corporations. The Purity Stores, Inc., however, attempted no such amendment of its articles and it took no such course because of its preference for a stock structure containing both par

value and non-par value stock. The Nevada corporation was organized to take over the property of the California corporation because under the Nevada law such a stock structure as was desired was permissible and because as this court truly observed the Nevada corporation “was incorporated for the sole and only purpose of preserving the stock structure adopted in California and which could not be maintained in California” (pp. 31, 32).

In making that choice in December, 1926, the Purity Stores, Inc. was acting freely and voluntarily and under no such compulsion as affected the B company in December of the year before. The Purity Stores, Inc. in December, 1926, knew that its *de facto* character was recognized by the courts and by the officials of California, knew that on paying its license fees it was entitled to a license to do business. It was subject to dissolution on *quo warranto* proceedings under Sec. 358 of the Civil Code but, though such proceedings were possible, the probability of such proceedings was very likely less of a moving factor in the decision of the Purity Stores, Inc. to incorporate in Nevada than the difficulty of securing a permit from the Corporation Commissioner to issue classes of stock which were not authorized by law. It was, as this court recognized, the desire to preserve a stock structure with par value stock and non-par value stock that lead to the Nevada incorporation proceedings. In December, 1926, the Purity Stores, Inc. had a free choice. It could abandon its existing stock structure and by amendment of its articles of incorporation provide for such a stock structure as could be maintained in California and

thus remain a California corporation and preserve its identity; or by entering a foreign jurisdiction it could create a new and foreign corporation with the stock structure desired and bring that foreign corporation into California to take over the business and assets of the domestic corporation. In deciding in favor of creating a foreign corporation it is apparent that the parties concerned deliberately intended to create a new and distinct corporate entity. The Nevada corporation had the power and authority to maintain a stock structure and to issue stock in accordance therewith which the domestic corporation lacked and this difference alone was sufficient to differentiate the California and the Nevada corporation not only in law but in fact as two separate and distinct entities and therefore not the same taxpayer within the meaning of Sec. 206(b) of the Revenue Act of 1926 (*Marr v. United States*, 268 U. S. 536, 541, 45 Sup. Ct. 575, 577). Looking through form to substance this essential difference between the two corporations still remained. The choice of the Purity Stores, Inc. made in December, 1926, was not affected by the conduct of state officials influenced by mistaken views of the law of the state, nor was it forced by a desire to escape possible criminal prosecution or to avoid possible litigation over the sanctity of its contracts. It was not a choice exercised under compulsion either in the same sense or in the same measure as was the choice of the B company in December, 1925, and there were therefore not special circumstances that would warrant bringing the Purity Stores, Inc. within the exception to the general rule declared in the *New Colonial Ice*

Co. case. It was simply a choice between changing its stock structure in conformity with the policy of the California law as set forth in its constitution or finding some way of doing business here as a corporation with a stock structure which did not conform to such a policy. The Purity Stores, Inc. had the way pointed in a decision rendered May 21, 1926. It learned from that decision that a foreign corporation with a stock structure composed of a par value and non-par value stock could enter California and do business here (*Commonwealth Acc. Corp. v. Jordan*, 198 Cal. 618, decided May 21, 1926).

The B company's procedure was in striking contrast to that of the Purity Stores, Inc. The B company did not attempt to find some way to maintain a stock structure opposed to the policy of the state. On the contrary, it attempted to change its stock structure to conform to that policy by appropriately amending its articles of incorporation. As a *de facto* corporation it had the legal right to so amend its articles, as was declared in the *Westlake Park Investment Co.* case (p. 618). Under the provisions of Sec. 362 of the Civil Code as amended in 1921, *supra*, any corporation had the right to amend its articles to provide for any "amendment not contrary to law". But this right was denied it by the Secretary of State when it attempted to exercise it. As a *de facto* corporation it was entitled to a license to do business in 1926. But this license was denied it by the Secretary of State. When thus denied its legal rights it sought as the only sure, prompt, and practical course in the premises within the time limits available to preserve the con-

tinuity of its business enterprise, the organization of the C company under California law with a stock structure in harmony with the laws of California and in line with what it had attempted to do through amendment of the articles of incorporation of the B company. In form the C company was a new entity of course. But in substance the C company was but a duplicate of what the B company would have been had it been permitted in 1925 to file its amended articles with the Secretary of State as it was legally entitled to do, but the right to do which was denied it. There was no motive in the case at bar to create a new corporate entity as the result of a free choice. The action was not voluntary in the sense that the action of those concerned was voluntary in the *Purity Inv. Co.* case and in the *New Colonial Ice Co.* case. There is a substantial distinction between the present case of the petitioner here and the *Purity Inv. Co.* case.

3. THE DISTINCTION BETWEEN THIS CASE AND THE NEW COLONIAL ICE CO. CASE.

The mere facts that the officers and stockholders of two corporations are substantially the same, that the two were organized for substantially the same purposes, and that the property and business enterprise of the one has been taken over by the other with no break in the continuity of the enterprise, with nothing more to establish the identity of the two, were held insufficient to establish the two corporations as a single taxpayer within the meaning of Sec. 204(b) of the Revenue Act of 1921 in the *New Colonial Ice Co.*

case where, as was the fact in that case, the transactions of the parties concerned producing that result were voluntary and where there was no exceptional situation justifying the court to look through form to substance and to recognize substantial identity in spite of formal diversity. But where circumstances might justify looking through form to substance it would be important that substantial similarity should be apparent.

If in the case at bar it be permitted, because of the exceptional situation, to look through form to substance, the substantial similarity between the B company and the C company is apparent. So far as such a factor has a bearing, that circumstance exists in the present case.

That there are occasions when the identity of two corporations as one will be recognized is, it is suggested, definitely stated in the *New Colonial Ice Co.* case. The petitioner in that case insisted (1) that “the continuity of the business was not broken by the transfer from the old company to the new”, (2) that “the ultimate parties in interest—stockholders and creditors—were substantially the same after the transfer as before”, and these contentions that court said might be conceded. The court replied to these contentions by saying, of the language of Sec. 204(b) of the Revenue Act of 1921,

“Taken according to their natural import they mean that the taxpayer who sustained the loss is the one to whom the deduction shall be allowed. Had there been a purpose to depart from the general policy in that regard, and to make the right

to the deduction *transferable or available to others than the taxpayer who sustained the loss*, it is but reasonable to believe that purpose would have been clearly expressed. And as the section contains nothing which even approaches such an expression, it must be taken as not intended to make such a departure'' (emphasis supplied).

It is obvious that up to this point in the decision the court is not considering the question whether the two corporations were substantially identical or whether, therefore, there was in substance only one taxpayer involved. The court up to this point was denying, without any consideration of alleged identity of the two corporations concerned, the right of a successor corporation to claim deductions in 1922 and 1923 for losses sustained by its predecessor corporation in 1921. This is even more obvious as the court proceeds with its opinion, for it says next,

''We come then to an *alternative* contention that, even though the section be not as broad as claimed, the deduction should be allowed, because 'for all practical purposes the new corporation was the same entity as the old one and therefore the same taxpayer' '' (emphasis supplied).

This alternative contention the court answered by saying,

''Thereafter neither corporation had any control over the other; the old corporation had no interest in the assets or business, and the chance of gain and the risk of loss were wholly with the new one. Thus the contention that the two corporations were practically the same entity and therefore the same taxpayer has no basis, unless, as

the petitioner insists, the fact that the stockholders of the two corporations were substantially the same constitutes such a basis.”

The contention of the petitioner that for all practical purposes the new corporation was the same entity as the old and therefore the same taxpayer was not to be conceded under the circumstances unless, as petitioner contended, the fact that the stockholders of the two corporations were substantially the same was a proper basis for the identity contention. The court did not recognize the mere identity of stock interests as establishing the identity of the two corporations in the *New Colonial Ice Co. Inc.* case but the court in that case has, we suggest, clearly indicated that there might be exceptional circumstances under which it would recognize the identity of stock interests as sufficiently establishing the identity of two corporations as the same taxpayer within the meaning of Sec. 204(b) of the Revenue Act of 1921 and therefore within the meaning of the similar Sec. 206(b) of the Revenue Act of 1926 with which the petitioner here is concerned.

The court in the *New Colonial Ice Co.* case met the last contention of the petitioner in that case by replying,

“As a general rule a corporation and its stockholders are deemed separate entities and this is true in respect of tax problems. Of course, the rule is subject to the qualification that *the separate identity may be disregarded in exceptional situations where it otherwise would present an obstacle to the due protection or enforcement of*

public or private rights. But in this case we find no such exceptional situation—nothing taking it out of the general rule. On the contrary, we think it a typical case for the application of that rule” (emphasis supplied).

In support of that reply the court cites among other cases, the following,

Southern Pacific Co. v. Lowe, 247 U. S. 330, 38 Sup. Ct. 540;

Gulf Oil Corporation v. Lewellyn, 248 U. S. 71, 39 Sup. Ct. 35.

In the *Southern Pacific Company* case, that company owned all the stock of the Central Pacific Railway Company, including the stock registered in the names of the directors. A dividend declared by the latter in favor of the former out of surplus accrued prior to March 1, 1913, was held not to be taxable income of the former. Such a dividend the court found to be income in form only and not taxable. As the court said, “the Central Pacific and the Southern Pacific were in substance identical because of the complete ownership and control which the latter possessed over the former, as stockholder and in other capacities. While the two companies were separate legal entities, yet in fact, and for all practical purposes they were merged, the former being but a part of the latter, acting merely as its agent and subject in all things to its proper direction and control”.

In the *Gulf Oil Corporation* case, that company owned all the capital stock of certain other corporations concerned except the qualifying shares held by

directors. What was a dividend to the parent company in form was held not taxable income in fact. "It is true", the court said, "that the petitioner and its subsidiaries were distinct beings in contemplation of law, but the facts that they were related as parts of one enterprise, all owned by the petitioner, that the debts were all enterprise debts due to members, and that the dividends represented earnings that had been made in former years and that practically had been converted into capital, unite to convince us that the transaction should be regarded as bookkeeping rather than as 'dividends declared and paid in the ordinary course by a corporation'. *Lynch v. Hornby*, 247 U. S. 339, 38 Sup. Ct. 543, 62 L. Ed. 1149. The petitioner did not itself do the business of its subsidiaries and have possession of their property as in *Southern Pacific v. Lowe*, 247 U. S. 330, 38 Sup. Ct. 540, 62 L. Ed. 1142, but the principle of that case must be taken to cover this".

In the *Southern Pacific Company* case and in the *Gulf Oil Corporation* case the fact that the earnings out of which the dividends were declared had been made prior to March 1, 1913, under the principles of *Lynch v. Hornby*, supra, would have been no saving factor, were it not for the further fact that the circumstances of those cases justified looking beyond the separate technical entities to the substantial identity of parent and subsidiary companies. In these two cases the court did look through form to substance in applying the income tax laws. It did recognize the substantial identity of the

two corporations concerned in those two cases and enforced a practical application of the income tax laws with the recognition of the substantial identity of two corporations as the controlling factor.

In a number of cases the Supreme Court has declared that in applying income tax laws substance and not form should be regarded. Thus in *United States v. Phellis*, 257 U. S. 156, 42 Sup. Ct. 63, the court said:

“We recognize the importance of regarding matters of substance and disregarding forms in applying the provisions of the Sixteenth Amendment and income tax laws enacted thereunder. In a number of cases besides those just cited we have under varying conditions followed the rule.”

In *Weiss v. Stearn*, 265 U. S. 242, 44 Sup. Ct. 490, the court said:

“Questions of taxation must be determined by viewing what was actually done, rather than the declared purpose of the participants, and when applying the provisions of the Sixteenth Amendment and income laws enacted thereunder we must regard matters of substance and not mere form.”

It is true that the decisions in the above cited cases announcing the substance rule were concerned with the taxation of gains or alleged gains by stockholders through stock dividends and for that reason are not directly apposite here.

But it is suggested that when a case arises which by reason of an exceptional situation would not come

within the general rule applied in the *New Colonial Ice Co.* case but rather within the exception to that rule there acknowledged, the principle applied in other cases that substance and not form is to control would be applicable to such an exceptional case. This principle was not repudiated in the *New Colonial Ice Co.* case. On the contrary, it was declared in effect that there are cases where “for the protection of private rights” as the court phrased it, the identity of two corporations may be recognized, and their separate technical entities may be disregarded.

In the case of *McCann v. Children’s Home Society*, 176 Cal. 359, the Children’s Home Society of California was a charitable and benevolent organization. In December 1891, the persons conducting this organization had attempted to form a corporation under the provisions of Secs. 593 et seq. of the Civil Code. By the provisions of Sec. 594, Civil Code, as they read in 1891, the articles of incorporation of such a corporation had to contain a verified statement showing certain facts relative to the election of its officers. The articles of incorporation were duly filed and a certificate of incorporation was duly issued by the Secretary of State. “Thereupon said Children’s Home Society of California carried on business as a corporation until 1908, when it was discovered that the original filing of articles of incorporation was invalid for want of the verification required by Sec. 594 of the Civil Code.” The Children’s Home Society of California, upon making the discovery noted in 1908, realized that it was not a *de jure* and was at

most a *de facto* corporation. Thereupon it caused new articles of incorporation to be filed in 1908, and took the other necessary steps to form a corporation under the laws of California by the same name "Children's Home Society of California".

The court found that the old corporation was not a *de jure* corporation, but that it was a corporation *de facto* (p. 363).

Various questions were raised in the case, one of them resting upon the claim that the old and new corporations were two separate and distinct entities. Upon this phase of the case the court said:

"Throughout his brief the appellant insists upon treating the organization which attempted to file articles in 1891 as an entity separate and distinct from the corporation which was formed in 1908. In discussing the legal points made, we have gone upon the assumption that this position was well founded. It is proper to say, however, that the real situation disclosed by the evidence is that the same persons who were conducting the organization from 1891 to 1908 filed articles of incorporation in the latter year for the purpose of correcting the defects in the attempted incorporation of 1891. In fact the new corporation was a continuation of the then existing *de facto* corporation, and we are satisfied that if the question were material here, there would be no substantial difficulty in perceiving and declaring that the two organizations were in reality identical."

In this case the situation of the petitioner is even stronger than that of the second corporation in the *McCann* case. Here the C company had as the sole

15 Fletcher Cyc. Corp. Perm. Edit.

(a) Section 7204. "Reincorporation **** is not the same thing as reorganization **** Reincorporation **** consists in the taking out of a new charter by a corporation in order to correct errors or defects in the original incorporation or to enlarge the powers or limit the liabilities of the corporation, or to lengthen or revive the corporate life. In a sense it is but an amendment of the charter, and, generally under the statutes there is no new corporation but the company is the same as before the reincorporation."

(b) Section 7285. **** "A reorganization, as distinguished from a mere reincorporation, generally results in the bringing into existence of a new corporation with the consequent dissolution of the old one."

(c) Section 7286. **** "However reincorporation, as the term has already been defined does not, ordinarily, create a new corporation. Thus the filing of articles of incorporation to correct defects in a former attempted incorporation makes the new corporation merely a continuation of the existing de facto corporation."

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motive for its origin a desire on the part of the parties concerned to protect their rights and to correct a defect in the articles of incorporation of the B company, a defect which the B company was entitled to correct through the amendment of its articles, but which, when it attempted to assert that right, was denied that privilege by the Secretary of State. If the California court in the *McCann* case would find no substantial difficulty in declaring the two corporations in form identical in reality, it can hardly be doubted that it would find no difficulty in declaring the B company and the C company in reality identical.

If, for the protection of private rights, courts are ever warranted in looking through form to substance and in recognizing the actual identity of two corporations as one and the same for any purpose, this case, it is suggested in all earnestness, is such a case.

The case at bar, we submit, is a case where under the exceptional situation which exists here the substantial identity of the B company and the C company may be recognized and where the two for the purposes of Sec. 206(b) of the Revenue Act of 1926 may therefore be recognized as the same taxpayer.

Such a recognition would call for a reversal of the decision of the Board of Tax Appeals, which rested wholly on the ground that the two corporations concerned were not, for the purpose of applying the income tax act, a single entity.

The balance of this brief is concerned wholly with the question of the petitioner's loss, when it was realized and what was its amount. If the court can-

not concur with the decision of the Board of Tax Appeals on the subject matter of corporate identity, the settlement of any question here about the loss remains for determination. If, on the contrary, the court concurs in the conclusion of the Board, the balance of this brief concerns a question which then need not be determined by the court.

4. **WHEN THE LOSS WAS REALIZED. THE LOSS OUT OF WHICH THE STATUTORY NET LOSS ASSERTED BY THE C COMPANY ARISES WAS NOT REALIZED SO AS TO FORM THE BASIS FOR TAXABLE LOSS OR GAIN UNTIL THE SALE BY THE B COMPANY IN 1925 OF THE KOSTER PRODUCTS COMPANY STOCK.**

- (a) This loss was not realized upon the transfer of the **A** company to the **Koster Products Company** on **May 31, 1919**.

As of May 31, 1919, the **A** company transferred to the **Koster Products Company**, a Nevada corporation, certain timber lands and plant in Oregon and Washington (Trans. pp. 39, 40, pars. 2, 3) whose adjusted cost at that time as stipulated was at least \$738,374.21, if certain carrying charges were not a proper element of cost (Trans. pp. 51, 52 and 53). In consideration of this transfer the **A** company received 8000 shares of the capital stock of the **Koster Products Company** on the basis of a value of \$50.00 per share, which was its fair market value at that time, making a total value of \$400,000.00 (Trans. pp. 39 to 41, pars. 3, 4, 5, 6). The **A** company in its return for its fiscal year then ending June 30, 1919, claimed a loss on this sale, which was disallowed by the Commissioner of Internal Revenue on the ground

that the two companies were then affiliated and the transaction accordingly an inter-company one in which there could be no taxable loss or gain (Ex. 4, Schedule K, explanation of Balance Sheet). At the time of this transaction, May 31, 1919, the A company owned 84.29 per cent of the stock of the Koster Products Company and stockholders of the A company held 11.23 per cent of the stock of the Koster Products Company, between them thus holding more than 95 per cent of the stock of the latter company (Trans. p. 40, par. 5). There is nothing in the record before the Board or this court to establish that the A company did not actually control this 11.23 per cent of the stock held by its stockholders or that such actual control was not legally enforceable. The ruling of the Commissioner is presumptively correct and the petitioner relied and still relies upon that presumption. That ruling necessarily involved the Commissioner's determination that the A company owned directly or controlled through closely affiliated interests substantially all of the stock of the Koster Products Company, or that substantially all of the stock of the two companies was owned or controlled by the same interests (Sec. 240 (b), Revenue Act of 1918). This ruling made out a prima facie case of affiliation (*United States v. Rindskopf*, 105 U. S. 418, 422). The burden of overcoming this presumption, of impeaching this prima facie case of affiliation is on the respondent (*Germantown Trust Co. v. Lederer*, 263 Fed. 672, 676, 8th Cir.). Any attack on that ruling in this proceeding is a collateral and not a direct attack. There is nothing in the record here to overcome the

presumption of affiliation and the conclusion that the transaction was an intercompany one accordingly in which no taxable gain or loss was realized.

It was compulsory under Sec. 240(a) of the Revenue Act of 1918 for affiliated companies to file consolidated returns and not optional as under later acts. By the provisions of Treasury Regulations No. 45, Art. 636, inter-company transactions were to be eliminated in determining the combined taxable income of the affiliated corporations. There could, therefore, be no taxable gains or losses arising from such inter-company transactions.

(b) The loss was not realized upon the transfer by the A company to the B company on August 28, 1924.

On August 28, 1924, the A company transferred all of its assets and business, including said 8000 shares of stock of the Koster Products Company, to the B company for preferred and common stock of the latter (Trans. p. 42, par. 8) under circumstances which amounted to a reorganization within the meaning of Sec. 203 of the Revenue Act of 1924 in which, accordingly, no taxable gain or loss could be recognized.

Where a corporation like the A company transferred property to another company like the B company for its capital stock under the provisions of Sec. 204(a) (7) of the Revenue Act of 1924 (corresponding to Sec. 204(a) (7) of the Revenue Act of 1926 and to Sec. 113(a) (7) of the Revenue Act of 1932), the basis of the property in the hands of the transferee corporation (the B company) is the same

as it would be in the hands of the transferor (the A company).

L. H. Philo Corporation v. Commissioner, 16

B. T. A. 130, 50 Fed. (2d) 1079;

Mente & Co. v. Commissioner, 24 B. T. A. 401;

Flushing Nurseries Co. v. Commissioner, 25 B.

T. A. 938;

Ridgewood Cemetery Co. v. Commissioner, 26

B. T. A. 626;

Newman, Saunders & Co. v. United States, 36

Fed. (2d) 1009; 281 U. S. 760; 50 Sup. Ct.

460;

Osburn California Corp. v. Welch, 39 Fed. (2d)

41; 282 U. S. 850; 51 Sup. Ct. 28.

The A company transferred all its assets to the B company in 1924 (Trans. p. 42, par. 8). Immediately thereafter the A company and its stockholders were in control of the B company, owning all of the capital stock of the B company, common and preferred, and all of the voting stock thereof (Trans. pp. 41, 42, pars. 7, 8). Both the common and preferred shares of the B company had voting rights (Trans. p. 41, par. 7). In consideration of the transfer to the B company, nine thousand (9000) shares of preferred stock of the B company were issued to the A company (Trans. p. 42, par. 8) and at the same time nine hundred ninety-five (995) shares of common stock of the B company issued to the stockholders of the A company, as its nominees (Trans. p. 42, par. 8). At the same time five shares of the common stock of the B company issued as qualifying shares to the directors and incorporators of the B company, who were also

directors of the A company (Trans. p. 42, par. 8). These five directors of the A company and of the B company were stockholders of the B company and, under California law, had to be stockholders of the A company. The remaining authorized capital stock of the B company remained unissued (Trans. p. 42, par. 8). Thus nine thousand (9000) shares of stock, preferred, was owned by the A company and one thousand (1000) shares of stock, common, was owned by the stockholders of the A company. The A company alone immediately after the transfer owned ninety per cent (90%) not only of all the voting stock, but of all the stock. An eighty per cent (80%) interest was sufficient to bring the A company and the B company within the provisions of Sec. 204 (a) (7) of the Revenue Act of 1924.

Such a situation constitutes a "reorganization", as defined by Sec. 203 (h) (1) (B) and Sec. 203 (i) of the Revenue Act of 1924. This situation also reveals both the A and the B company as a "party to a reorganization" within the meaning of the Revenue Act of 1924 (Sec. 203 (h) (1) (B) and (h) (2)). The B company resulted from the reorganization. It was created by the directors of the A company (Trans. p. 42, par. 8) for the same purpose as the A company, namely, to engage in the manufacture and sale of barrels and cooperage (Trans. p. 41, par. 7). No stock was issued by the B company, not even the qualifying shares of its directors until the transfer to it of the assets of A company (Trans. p. 42, par. 8). This transfer was made under authority not only of the directors and stockholders of the A company, but

of all of its creditors (Trans. p. 42, par. 8). The transfer was made so that the business enterprise formerly conducted by the A company might be continued by the B company, free from the load of debt pressing on the A company, in the form of a stockholder's liability, the B company converting that into a capital stock liability, and thereby enjoying a better credit position for current obligations, than the A company had (Trans. p. 43, par. 9). Every step taken from the first formation of the B company to the final transfer to it of the assets of the A company and the resulting stock issues and the attendant trust agreement with the bank reveals a definite plan of reorganization to provide for those creditors whose claims were predicated on a stockholder's liability of the A company and to improve the credit position of the business enterprise. Not only did the B company thus result from the reorganization and become a party to it but the A company, acquiring ninety per cent (90%) not only of the voting stock, but of the total number of shares of all classes of stock, also became a party to the reorganization, within the meaning of the Revenue Act of 1924.

By the provisions of Sec. 203 (b) (3) of the Revenue Act of 1924, no gain or loss shall be recognized if a corporation a party to a reorganization—the A company—exchanges property in pursuance of the plan of reorganization, solely for stock or securities in another corporation a party to the reorganization—the B company. Except as the B company agreed to assume certain debts of the A company the sole consideration for the transfer was the stock

of the B company (Trans. pp. 42, 43, pars. 8, 9). By the provisions of Sec. 203 (f) if an exchange would be within the provisions of Sec. 203 (b) (3), just referred to, if it were not for the fact that the property received in exchange consists not only of property (stocks and securities) permitted by such paragraph to be received without the recognition of gain or loss, but also of other property or money, then no loss from the exchange shall be recognized.

It is self-evident, therefore, that no taxable gain or deductible loss resulted from the transfer from the A company to the B company in 1924, and that the B company under Sec. 204 (a) (7) of the Revenue Act of 1924 was entitled on a future sale of the eight thousand (8,000) shares of the Koster Products Company to use the same base for determining the loss thereon as the A company.

The B company party to this reorganization though not a *de jure* was a *de facto* corporation and within the terms of the Westlake Park Investment Co. opinion heretofore referred to. The B company as a *de facto* corporation used its franchise as shown by its income tax returns for 1924 and 1925 (Ex. 2 and 4). The very issue of stock in 1924 is evidence of a user of its franchise and of its *de facto* character (*Midwest Air Filters Pacific Inc. v. Finn*, 201 Cal 587, 592; *Tulare Irr. Dist. v. Shepard*, 185 U. S. 1, 22 Sup. Ct. 531). As a *de facto* corporation it must, for all the purposes of this case, be recognized as a corporation within the meaning of Sec. 203 of the Revenue Act of 1924. A *de facto* corporation is not only a corporation in fact but also in law (*People v. La Rue*,

67 Cal. 526, 530; *McCann v. Childrens Home Society*, 176 Cal. 359, 363, *Ballantine Private Corporations* (1927) Sec. 26). The B company therefore though a *de facto* corporation, was a corporation and a party to a reorganization within the meaning of Sec. 203 of the Revenue Act of 1924 as fully as though it had been a *de jure* corporation.

The loss not having been realized in 1919 nor in 1924 the first occasion when a realizable loss could be asserted for the purpose of determining taxable gain or loss within the meaning of the Revenue Acts concerned, was on the sale of the shares of the Koster Products Co. by the B company in 1925.

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5. THE AMOUNT OF THE LOSS, THE FACTS BEING STIPULATED, IS A QUESTION OF LAW. THE LOSS REALIZED ON THE SALE OF STOCK IN 1925 BY THE B COMPANY WAS SUFFICIENT AFTER THE DEDUCTION OF A STATUTORY NET LOSS BY THE C COMPANY IN ITS RETURN FOR 1927 TO LEAVE A PORTION OF THAT STATUTORY NET LOSS STILL UNEXTINGUISHED.

Whether we take as the basis for determining gain or loss the adjusted cost of \$908,201.85 used by the C company, which included carrying charges as one of the elements thereof, or the lower figure of \$738,374.21 exclusive of those carrying charges, the net result is the same for in either case the resulting statutory net loss deductible from the 1927 income of the C company was more than sufficient to result in no tax (see Appendix E to this brief). The facts of this case are not in dispute. The case was by stipulation submitted on an agreed statement of facts.

Under such circumstances, had the board found facts not supported by the stipulation, it would be “the duty of the court to accept as the facts those disclosed by the stipulation and not the facts as found by the Board of Tax Appeals” (*Iowa Bridge Co. v. Commissioner*, 39 Fed. (2d) 777, 780—8th Cir.).

This case therefore can be fully adjudicated by this court. The question as to the amount of loss can be determined as a matter of law from the facts which have been stipulated. Upon this review of the order of the Board this court has “power to affirm or, if the decision of the Board is not in accordance with law to modify or reverse the decision of the Board, with or without remanding the case for a rehearing, as justice may require” (26 U. S. C. A., Sec. 1226, Sec. 1003, 44 Stat. 110).

By the agreed statement of facts it was stipulated that the adjusted cost of the properties of the A company as of May 31, 1919, which on that date was transferred to the Koster Products for its shares of stock, was as set forth in Exhibit 1 attached thereto and incorporated therein by reference (Trans. p. 39, pars. 2, 3). That Exhibit 1 (Trans. pp. 52 and 53) fixed that adjusted cost, less depletion and depreciation, at \$738,374.21, exclusive of carrying charges, and conceded that the carrying charges amounted to \$169,827.64. The petitioner believed that as a matter of law these carrying charges should be included as an element of adjusted cost which would raise the figure to \$908,201.85. For the purposes of this review the lower figure of \$738,374.21 may be accepted without

any change in the result. It is true that the Oregon lands were acquired in 1919 and the other property in 1918, and that original cost, less depletion and depreciation, was the basis of reaching the stipulated adjusted cost. The question of adjusted cost was a factor in determining taxable loss on the sale of the stock of the Koster Products Company in 1925 by the B company and at that time the basis for determining gain or loss was declared in Sec. 204 (b) of the Revenue Act of 1924, which provided as follows,

“The basis for determining the gain or loss from the sale or other disposition of property acquired before March 1, 1913 shall be (A) the cost of such property * * * or (B) the fair market value of such property as of March 1, 1913 whichever is greater.”

Cost, therefore, was the proper basis to be used as to all the property acquired in 1918 (after March 1, 1913). As to the Oregon property acquired in 1910, (before March 1, 1913) the proper basis was cost if that was the higher, or the fair market value as of March 1, 1913, if that was the higher. If the cost of the Oregon property was higher than its fair market value as of March 1, 1913, the cost was the proper basis. If its cost was lower than the fair market value the only one affected by using cost instead of value is the petitioner whose loss under those circumstances would be understated rather than overstated. The basis for determining taxable gain or loss to the B company in 1925 may therefore be taken at \$738,374.21, which less the \$64,400.00 received for the stock

in 1925 makes a net loss of \$673,974.21 and a statutory net loss in 1925 of \$332,015.02 subject to carry over in 1926 and 1927, more fully shown in Appendix E, and more than sufficient to result in no tax to the C company on its 1927 income. If the A company had retained the Koster Products Company stock and sold it in 1925 for \$64,400.00 the basis for establishing its net loss on that sale would have been \$738,374.21. When the B company acquired this stock from the A company in 1924 in a transaction which amounted to a reorganization under Sec. 203 of the Revenue Act of 1924, upon the sale by the B company of this stock in 1925 for \$64,400.00 its basis, too, for establishing its net loss on that sale was \$738,374.21 (Sec. 204 (a) (7) of the Revenue Act of 1924).

The petitioner argued before the Board that the provisions of Sec. 204 (a) (7) of the Revenue Act of 1924 were not applicable because that section excluded "stock or securities in a corporation a party to a reorganization" and because he claimed that the Koster Products Company was a party to the reorganization resulting from the transfer from the A company to the B company in 1924 and that therefore only \$15.00 per share was the proper basis of cost of this stock in determining loss on its sale in 1925. There is no point in this claim, if the Koster Products Company was not "a party to a reorganization". The Koster Products Company was not in fact nor in any fair interpretation of Sec. 203 of the Revenue Act of 1924 a party to the reorganization. The only parties to the reorganization in 1924 were the A company and the

B company, the only actors therein. In that reorganization the Koster Products Company was not consulted, nor was it in any way an active participant therein, nor did it receive anything therefrom.

Whether the respondent will renew that claim before this court we are not at present advised. If he does, we should like the privilege of answering him here as we did before the Board. We will not make further answer to this possible claim in the main text of this brief, but we have set forth our answer to that contention in Appendix D to this brief, not desiring to take the time of the court unnecessarily, if the point is not made, but preserving the right to make the reply thereto set forth in Appendix D, if the point should be made before this court.

IV.

CONCLUSION.

The circumstances of this case distinguish it, we submit from the *New Colonial Ice Co.* case and the *Purity Inv. Co.* case. They are, we believe, sufficient to warrant the recognition of the B company and the C company as a single entity and as the same taxpayer within the meaning of Sec. 206 (b) of the Revenue Act of 1926. The amount of the loss carried over as a statutory net loss in 1927 was more than sufficient to result in no tax for that year.

The court is accordingly requested to modify the order of the Board assessing a deficiency tax against

the petitioner in the sum of \$14,915.65 and to adjudge, on the contrary, that there is no tax due or owing by the petitioner on its 1927 income.

Dated, San Francisco,
October 4, 1935.

Respectfully submitted,

ALLEN G. WRIGHT,

RANDELL LARSON,

Counsel for Petitioner.

(Appendices A, B, C, D and E Follow.)

(Appendices **A**, **B**, **C**, **D** and **E** Follow.)

Appendix A

PERTINENT EXTRACTS FROM REVENUE ACTS INVOLVED, NOT SET FORTH IN BRIEF.

1. *Revenue Act of 1918.*

Sec. 240 (b). For the purpose of this section two or more domestic corporations shall be deemed to be affiliated (1) if one corporation owns directly or controls through closely affiliated interests or by a nominee or nominees substantially all the stock of the other or others, or (2) if substantially all the stock of two or more corporations is owned or controlled by the same interests.

2. *Revenue Act of 1924.*

Sec. 203 (b) (3). No gain or loss shall be recognized if a corporation a party to a reorganization exchanges property, in pursuance of the plan of reorganization, solely for stock or securities in another corporation a party to the reorganization.

Sec. 203 (f). If an exchange would be within the provisions of paragraph (1), (2), (3), or (4) of subdivision (b) if it were not for the fact that the property received in exchange consists not only of property permitted by such paragraph to be received without the recognition of gain or loss, but also of other property or money, then no loss from the exchange shall be recognized.

Sec. 203 (h) (1). The term "reorganization" means (A) a merger or consolidation (including the

acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation), or (B) a transfer by a corporation of all or a part of its assets to another corporation if immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred, or (C) a recapitalization, or (D) a mere change in identity, form, or place of organization, however effected.

Sec. 203 (h) (2). The term "a party to a reorganization" includes a corporation resulting from a reorganization and includes both corporations in the case of an acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation.

Sec. 203 (i). As used in this section the term "control" means the ownership of at least 80 per centum of the voting stock and at least 80 per centum of the total number of shares of all other classes of stock of the corporation.

Sec. 204 (a). The basis for determining the gain or loss from the sale or other disposition of property acquired after February 28, 1913 shall be the cost of such property. * * *

(7) If the property (other than stock or securities in a corporation a party to the reorganization) was acquired after December 31, 1917, by a corporation in

connection with a reorganization, and immediately after the transfer an interest or control in such property of 80 per centum or more remained in the same persons or any of them, then the basis shall be the same as it would be in the hands of the transferor, increased in the amount of gain or decreased in the amount of loss recognized to the transferor upon such transfer under the law applicable to the year in which the transfer was made.

Appendix B

PERTINENT EXTRACTS FROM CERTAIN CALIFORNIA CODE SECTIONS.

1. CALIFORNIA CIVIL CODE SECTIONS 290 b, 290 c, 290 d, 290 e
AND 290 f, AS AMENDED STATS. 1923, p. 621, CHAP. 293.

Sec. 290b. Any private corporation created and existing or authorized to be created under the provisions of title one, part four, division first of the Civil Code may, if so provided in its articles of incorporation or in any amendment thereof, issue shares of stock of such corporation (other than stock preferred as to dividends or as to its distributive share in the assets of the corporation) without any nominal or par value by stating in its articles of incorporation or in such articles as so amended:

(a) The number of shares with a nominal or par value, if any, and the number of shares without a nominal or par value that may be issued by the corporation, and the classes, if any, into which such shares are to be divided, together with a statement of the distinguishing preferences, rights, privileges and restrictions of each class;

(b) The nominal or par value (which shall be the same for all shares, having a nominal or par value) of shares other than shares which it is stated are to have no nominal or par value;

(c) Either (1) the amount of stated capital with which the corporation will begin business, which amount shall not be less than five hundred dollars; and

that the corporation will carry on business with a stated capital which shall not be less than the aggregate amount of the preference to which all issued and outstanding stock having a preference as to principal is entitled, and in addition thereto an amount therein stated in respect to every share of stock issued and outstanding other than stock having a preference as to principal, which amount shall not be less than five dollars for each share, and such additional amount as from time to time may by resolution of the board of directors of the corporation be transferred thereto; or (2) the amount of stated capital with which the corporation will begin business, which in no event shall be less than five hundred dollars; and that the corporation will carry on business with a stated capital consisting of the aggregate of the amounts received by it as consideration for the issuance of its shares with no nominal or par value, the aggregate par value of all issued and outstanding shares, if any, having a nominal or par value, and such additional amounts as from time to time may by resolution of the board of directors of the corporation be transferred thereto.

Such statements in the articles of incorporation or such articles as amended shall be in lieu of any statements prescribed by the law under which the corporation shall have been formed as to the maximum amount of its capital stock or the number of shares into which the same shall be divided or the amount of the par value of such shares.

Subject to the preferences, rights, limitations, privileges and restrictions lawfully granted or imposed in

respect of any stock or class thereof, each share of such stock with no nominal or par value shall be equal to every other share of such stock. Every certificate for such shares without nominal or par value shall have plainly written or printed upon its face the number of such shares which it represents, and no such certificate shall express any nominal or par value of such shares or express any rate of dividend in terms of percentage of any nominal or par value. The certificates for preferred shares shall state the amount, if any, which the holders of each of such preferred shares shall be entitled to receive on account of principal from the assets of the corporation in preference to the holders of other shares, and shall state briefly any other rights or preferences given to the holders of such shares.

Subject to laws creating and defining the duties of the commissioner of corporations and to the law creating and defining the duties of the railroad commission, such corporation may issue and may from time to time sell its authorized shares without nominal or par value for such consideration as may be prescribed in the articles of incorporation or for such consideration as shall be the fair market value of such shares, and in the absence of fraud in the transaction the judgment of the board of directors as to such value shall be conclusive; or in the absence of fraud in the transaction, for such consideration as from time to time may be fixed by the board of directors pursuant to authority conferred in such articles of incorporation; or for such consideration as shall be consented to or approved by the holders of a majority of shares

then outstanding at any meeting called in the manner prescribed by the by-laws of such corporation, provided the call for such meeting shall contain notice of such purpose. Any and all shares issued as permitted by this section shall be deemed fully paid, and the holder of such shares shall not be liable to the corporation in respect thereof.

Sec. 290c. No corporation authorized to issue shares with no nominal or par value shall begin business until the amount of capital with which it will begin business, as stated in its articles of incorporation or in its articles of incorporation as amended, shall have been fully paid in, nor shall any such corporation, until the capital with which it will carry on business, as stated in its articles of incorporation or its articles of incorporation as amended, shall have been fully paid in, incur any debts in excess of the amount of stated capital paid in at the time such debts are contracted. In case of the increase of the stated capital with which the corporation will carry on business, such increase shall be deemed paid in to the extent of the amount of the assets which the corporation has in money and property in excess of the former stated capital. The directors of the corporation assenting to the creation of any debt in violation of this section shall be liable jointly and severally for the debts of such corporation; but no action shall be brought under the foregoing provision of this section unless within one year after the debt shall have been incurred the creditors shall have served upon the director written notice of intention to hold him personally liable for such debt. Any director who, because of any such

liability under this section, shall pay any debt of the corporation shall be subrogated to all rights of the creditor in respect thereof against the corporation and its property and also shall be entitled to contribution from all other directors of the corporation similarly liable for the same debt and the personal representatives of any such director who shall have died before making such contribution.

Unless it shall have been first permitted or authorized so to do by the commissioner of corporations, no such corporation shall declare or pay any dividend which shall reduce the amount of its stated capital. In case any such dividend shall be declared, the directors in whose administration the same shall have been declared, except those who may have caused their dissent therefrom to be entered upon the minutes of any meeting of the directors at which such action was taken or who were not present when such action was taken, shall be liable jointly and severally to such corporation and to the creditors thereof to the full amount of any loss sustained by such corporation or by its creditors by reason of such dividend.

Sec. 290d. For the purpose of fixing the fee prescribed by section four hundred nine of the Political Code for filing the articles of incorporation of any corporation formed under section two hundred ninety b of this code, the shares of stock of such corporation having no nominal or par value shall be taken to be of the par value of one hundred dollars.

Sec. 290e. In case of any such corporation having capital stock with nominal or par value and capital

stock without nominal or par value, no distinction shall be made between the classes of stock either as to voting power or as to the statutory or constitutional liability of the holders thereof to the creditors of the corporation.

Sec. 290f. Any private corporation formed under the provisions of title one, part four, division one of the Civil Code and now existing or which may hereafter be incorporated under said title may amend its articles of incorporation for the purpose of adopting the provisions of sections two hundred ninety b, two hundred ninety c, two hundred ninety d, two hundred ninety e and two hundred ninety f of the Civil Code, in the manner set forth by the provisions of section three hundred sixty-two of the Civil Code of California as amended.

**2. CALIFORNIA CIVIL CODE SECTION 305, AS AMENDED
STATS. 1905, p. 503, CHAP. 392.**

305. * * * Directors of corporations for profit must be holders of stock therein to an amount to be fixed by the by-laws of the corporation * * *

**3. CALIFORNIA CIVIL CODE SECTION 362, AS AMENDED 1921,
p. 134, CHAP. 134.**

362. Any corporation organized under the laws of this State may amend its articles of incorporation for any or all of the following purposes:

(1) To set forth a new name.

* * * * *

(8) And generally to provide for any other amendment not contrary to law.

* * * * *

Upon the adoption of amended articles of incorporation, a copy of the articles as thus amended shall be certified to as correct by the president and secretary and a majority of the directors of the corporation * * *

The copy of amended articles of incorporation thus certified shall be filed in the office of the secretary of state, whereupon such corporation shall have the same powers and the stockholders thereof shall thereafter be subject to the same liabilities as if such amendment had been embraced in the original articles of incorporation.



4. CALIFORNIA CODE OF CIVIL PROCEDURE, SECTION 1227, AS AMENDED STATS. 1880, p. 109, CHAP. 86, AND SECTION 1228, AS AMENDED STATS. 1907, p. 318, CHAP. 254.

1227. A corporation may be dissolved by the Superior Court of the county where its principal place of business is situated upon its voluntary application for that purpose.

1228. The application must be in writing and must set forth

1. * * *

2. That all claims and demands against the corporation have been satisfied and discharged.

Appendix C

PERTINENT EXTRACTS FROM CALIFORNIA CORPORATION LICENSE ACT (STATS. 1915, p. 422, CHAP. 190, AS AMENDED STATS. 1917, p. 371, CHAP. 215).

* * * Sec. 3. Except those corporations hereinafter specified, every corporation incorporated under the laws of this state, and every corporation incorporated under the laws of any other state, territory, or foreign country now doing intrastate business within this state, or which shall hereafter engage in intrastate business in this state, shall procure annually from the secretary of state a license authorizing the transaction of such business in this state, and pay therefor the license tax prescribed herein.

* * * Sec. 4. The license hereby provided authorizes the domestic corporations holding the same to transact business in this state, and authorizes foreign corporations to transact intrastate business in this state, during the year or any fractional part of such year for which such license is issued. "Year" within the meaning of this act, means from and including the first day of January to and including the thirty-first day of December next thereafter.

* * * Sec. 6. Corporations organized and conducted solely and exclusively for educational, religious, scientific or charitable purposes, corporations which are not organized or conducted for profit, corporations organized under the laws of any other state, territory or foreign country doing solely and exclusively an interstate or foreign business, and those

corporations taxed under subdivisions (a), (b), and (c) of section fourteen of article XIII of the constitution, are exempt from payment of the tax provided by section three of this act.

* * * Sec. 11. After six o'clock p.m. of the Saturday preceding the first Monday in March in any year, the corporate rights, privileges and powers of every domestic corporation which has failed to pay the tax and money penalty for nonpayment thereof imposed by this act shall, from and after said hour of said day, be suspended, and incapable of being exercised for any purpose or in any manner, except to execute and deliver deeds to real property in pursuance of contracts therefor made prior to such time, and to defend in court any action brought against such corporation, until said tax with all accrued penalties, taxes and charges due to the state under this act and subdivision (d) of section fourteen, article XIII of the constitution are paid as hereinafter provided. The right and privilege of every foreign corporation, subject to the provisions of this act, to transact intrastate business in this state shall, for failure to pay the tax and money penalty for nonpayment thereof imposed by this act, be forfeited at said hour of said day, and the secretary of state shall make a record of such forfeiture. In the case of foreign corporations such forfeiture may be relieved and the corporation's privilege to transact intrastate business in this state restored in the manner hereinafter provided. After said hour of said day and until such taxes, penalties and charges are paid, every person who attempts or purports to exercise any of the

rights, privileges or powers of any delinquent domestic corporation except as permitted by this act, or, who transacts or attempts to transact any intrastate business in this state in behalf of any forfeited foreign corporation, shall be guilty of a misdemeanor and upon conviction thereof shall be punished by a fine of not less than two hundred fifty dollars and not exceeding one thousand dollars, or by imprisonment in the county jail not less than fifty days or more than five hundred days, or by both such fine and imprisonment. The jurisdiction of such offense shall be held to be in any county in which any part of such attempted exercise of such powers, or any part of such transaction of business was had or occurred. Every contract made in violation of this section is hereby declared to be void.

Appendix D

RESERVED ARGUMENT.

THE KOSTER PRODUCTS COMPANY WAS NOT A PARTY TO THE REORGANIZATION RESULTING FROM THE TRANSFER OF THE A COMPANY TO THE B COMPANY IN 1924.

The 8,000 shares of stock of the Koster Products Company which the A company transferred in 1924 to the B company and which had been previously acquired by the former at a cost of over \$92.00 per share, using \$738,374.21 as the base, did not at the time of their transfer in 1924 have a fair market value in excess of \$15.00 per share. The transfer from the A company to the B company of all the assets of the former including these 8,000 shares of stock being a transfer under a reorganization as defined in the Revenue Act of 1924 was one in which the A company could assert no loss, for income tax purposes under Sec. 203(b) (3) and Sec. 203(f) of that act. The consideration to the A company for this transfer was stock of the B company, its *alter ego*, issued to the A company and its stockholders, as its nominees. If the B company, as may be suggested by the respondent, had been obliged to carry this stock at a cost of only \$15.00 per share as the base for future gain or loss, on the later sale thereof, both companies would be forced to take a loss for which neither might secure any tax relief. The A company can assert no loss arising from the transfer in 1924 by reason of the reorganization in 1924, and the B company, owned by the same interests as the A company, on the sale of the stock in 1925, according to the respondent, would

be obliged to measure its loss with a cost of \$15.00 per share as the yard stick for measurement. If the A company had not been obliged to effect a reorganization in 1924, and had sold these 8,000 shares of stock in 1925, just as the B Company did for \$8.00 per share, the A company could have asserted a loss of \$84.00 per share. But because in the meantime there was a reorganization in the course of which these shares were transferred to the B company, the respondent may suggest that the only loss which the B company can assert is limited to \$7.00 per share. The difference between a loss of \$84.00 per share and \$7.00 per share would therefore be automatically erased from the record to the profit of the Government and the penalty of the taxpayer. As there is nothing unlawful or unethical *per se* in corporate reorganizations and as they are often economically necessary, the mind naturally recoils from such an interpretation of the Revenue Act of 1924 when such arbitrary and inequitable consequences must necessarily follow such an interpretation. In short, it does not seem credible that the reorganization provisions of the Revenue Act of 1924 were framed to penalize taxpayers who might be parties thereto. This naturally suggests a careful analysis of those provisions.

The respondent may suggest that the Koster Products Company was, under Sec. 203(h) (2) of the Revenue Act of 1924, a party to the reorganization of the A company and the B company effected in 1924, and that therefore the B company cannot, under Section 204(a) (7) of the Revenue Act of 1924, claim as the basis for future gain or loss on the sale of the

Koster Products Company stock the basis which it had in the hands of the transferor, the A company. The major premise of such an argument is that the Koster Products Company was a party to the reorganization. If it was not, the whole basis for the suggestion fails. It is our position that the Koster Products Company was not a party to the reorganization effected by the A company and the B company in 1924. The Koster Products Company was certainly not an actor in that reorganization and in any usual and commonly accepted meaning of the phrase it was not therefore a party to that reorganization.

In the analysis which follows, unless otherwise indicated, all references to sections and subdivisions thereof are to the Revenue Act of 1924.

Sec. 203(a) reads: "Upon the sale or exchange of property the entire amount of the gain or loss, determined under Section 202, shall be recognized, except as hereinafter provided in this section."

Unless, therefore, an exchange of property falls within some one of the exceptional cases provided for in the subdivisions which follow (a) in Section 203 the resulting gain or loss must be recognized. Subdivisions (b), (c), (d), (e), (f) and (g) of Section 203 are concerned with those exceptional cases. In some of the paragraphs of those subdivisions the term "reorganization" is used, in other paragraphs that term is absent. Wherever the term "reorganization" is used, it is necessary that the meaning of the term be clear; and a definition is found in subdivision (h) of Section 203. This definition, therefore, is obviously intended to clarify and make definite the term "reor-

ganization", wherever that term is used in the section; and this definition, as obviously, can have no other purpose. Any fair interpretation of the statutory definition of a "reorganization" must necessarily be related to the paragraphs of Section 203 which it is intended to make clear, plain and definite. The term "reorganization" is used in Section 203, in subdivision (b) in paragraphs (2) and (3), in subdivision (c), in subdivision (d) in paragraph (2), in subdivision (e) and in subdivision (g). Subdivision (d) in paragraph (1) refers to subdivision (b) in paragraph (2) where the term "reorganization" is used and subdivision (f) refers to subdivision (b) paragraphs (2) and (3) in both of which the term "reorganization" is used. Any definition of "reorganization" as that term is used in subdivision (b) in paragraphs (2) and (3) thereof would fully cover and explain all references to that term in the other paragraphs or subdivisions of Section 203, as the mere perusal of them will manifest. The two important paragraphs of Section 203 so far as the effect of a reorganization upon the recognition of loss or gain is concerned are paragraphs (2) and (3) of subdivision (b). The other paragraphs and subdivisions of Section 203 preceding the definition of subdivision (h) are either not concerned with the effect of a reorganization or are refinements of the general provisions of paragraphs (2) and (3) of subdivision (b).

Those two paragraphs of subdivision (b) read as follows:

"(2) No gain or loss shall be recognized if stock or securities in a corporation a party to a

reorganization are, in pursuance of the plan of reorganization, exchanged solely for stock or securities in such corporation or in another corporation a party to the reorganization.

“(3) No gain or loss shall be recognized if a corporation a party to a reorganization exchanges property, in pursuance of the plan of reorganization, solely for stock or securities in another corporation a party to the reorganization.”

Under the provisions of subdivision (b), paragraph (1) of Section 203 no gain or loss shall be recognized “if common stock in a corporation is exchanged solely for common stock in the same corporation, or if preferred stock in a corporation is exchanged solely for preferred stock in the same corporation”, and no gain or loss would be recognized on such limited exchanges quite apart from any question of reorganization. But if common stock in a corporation is exchanged solely for preferred stock in the same corporation, as might be the event in case of a recapitalization, gain or loss would be recognized, unless the exchange fell within the exception noted in paragraph (2) of subdivision (b). But that exception is limited to a case where there is a reorganization. In subdivision (h) of Section 203 it is provided that as used in that section the term reorganization, among other things, means a recapitalization.

Except as paragraph (2) of subdivision (b) covers certain cases of an exchange of stock or securities of a corporation solely for stock or securities of such corporation it is confined to cases of an exchange, pursuant to a plan of reorganization, of the stock or secu-

rities of one corporation solely for the stock or securities of another corporation, with the added condition that both corporations, parties to the exchange, must be parties to the reorganization. In such an exchange of stock of one corporation for the stock of another, it is obvious that both corporations are actors in the transaction and are parties to a contract of exchange.

Paragraph (3) of subdivision (b) is confined to cases of an exchange pursuant to a plan of reorganization of the property of one corporation solely for the stock or securities of another corporation, with the added condition that both corporations, parties to that exchange, must be parties to the reorganization. In such an exchange of the property of one corporation for the stock of another it is again evident that both corporations are actors in the transaction and are parties to a contract of exchange. Given a statutory definition of a reorganization there would be no difficulty in identifying the two corporations as parties to the reorganization who were parties to an exchange of the stock of the one for the stock of the other, or of the property of the one for the stock of the other, where the exchange was made pursuant to a plan of the reorganization.

To a full understanding of the scope of these two paragraphs (2) and (3) of subdivision (b) it is only necessary to have a clear and authoritative definition of the term reorganization.

An exchange of the stock or securities of one corporation for the stock or securities of another, or an

exchange of the property of one corporation for the stock or securities of another may be the form, in whole or in part, which a merger or a consolidation may take. Both a “merger” and a “consolidation” are included in the statutory definition of the term reorganization; Sec. 203, subdivision (h) (1) (A). There would therefore be no gain or loss recognized in an exchange either (1) of the stock or securities or (2) of the property of one corporation, party to a merger, solely for the stock or securities of another corporation, party to the merger, where the exchange was made pursuant to the plan of merger. And what is thus true of a merger would be equally true of a consolidation. There would, however, be no difficulty in identifying the two or more corporations, parties to such an exchange, as the parties to such a merger or consolidation and as therefore the parties to the statutory reorganization.

A corporation may also reorganize within the statutory definition, if it transfers all or a part of its assets to another corporation, if immediately after the transfer the transferor or its stockholders or both are in control of the corporation to which the assets are transferred—Sec. 203 (h) (1) (B)—and “control” means the ownership of at least 80 per centum of the voting stock and at least 80 per centum of the total number of all other classes of stock of the corporation—Sec. 203 (i). If a corporation, pursuant to a plan to that effect, transferred all of its property to another corporation solely in exchange for stock in the other corporation, and immediately after the transfer the first corporation was in the statutory

control of the second, there would be a statutory reorganization and there would be no gain or loss recognized in the exchange. There would be no difficulty in identifying these two corporations, parties to such an exchange, as the parties to the statutory reorganization.

If a corporation recapitalized, or effected a mere change in identity, form, or place of organization, such a change, though amounting to a statutory reorganization—Sec. 203 (h) (1) (D)—would have no effect upon the recognition of gain or loss unless in connection therewith there had been an exchange of stock or securities for stock or securities, or an exchange of property for stock or securities. If, as the result of a recapitalization noted in clause (C) or some of the other changes noted in clause (D), the only corporation concerned exchanged its own securities for its own stock or exchanged its own common for its own preferred stock, there would be no recognition of gain or loss, if it were a party to a reorganization. To avoid any difficulty which there might be in identifying such a single corporation as a party to such a reorganization as is recognized in clauses (C) and (D) which merely exchanged its own securities, Section 203 (i) declares in substance that the corporation emerging or resulting from a change in its capitalization, form, identity or place of organization, however effected, should be included in the term “a party to a reorganization”.

Thus subdivision (h) (1) defining a reorganization is concerned with two or more corporations dealing

with each other through exchanges of securities and property in the case of a "merger" or "consolidation" under clause (A), or in the case of a "transfer" under clause (B); and is concerned with a single corporation effecting a "recapitalization" under clause (C) or a "mere change in identity, form or place of organization, however effected" under clause (D).

Section 203 (h) (1) reads in part as follows, "The term 'reorganization' means (A) a merger or consolidation (including the acquisition by one corporation of at least a majority of the voting stock and at least a majority of the total number of shares of all other classes of stock of another corporation, or substantially all the properties of another corporation) or (B) etc.

It would be most surprising if the parenthetical addition of the "acquisition" clause to clause (A) were intended to cover any "acquisition" except that by way of an exchange of securities and properties between two corporations, similar in character, if not in degree, to the exchanges necessarily involved in a "merger" or a "consolidation". The fact that the "acquisition" clause was added to the "merger" and "consolidation" reference by way of parenthesis and that it is introduced by the significant word "including" suggests with further emphasis that the Congress had in mind in the "acquisition" clause merely another case of an exchange of property and securities between two corporations, having some of the practical characteristics, so far as gain or loss might be concerned, but lacking the complete form of a technical "merger" or "consolidation".

Mergers and consolidations are purely statutory in character. But the acquisition by one corporation of a majority of the voting and other classes of stock of another, or of substantially all of the properties of another corporation, while falling short of a technical merger or consolidation, is a situation in which it is equally as fair that no gain or loss should be recognized, where there was an exchange of stock of one corporation solely for stock of another, or an exchange of property of one corporation solely for stock of another, as in the case of a technical merger or consolidation.

It is difficult to believe that in the "acquisition" clause parenthetically included in clause (A) the Congress could have deliberately intended to define a "reorganization" in such broad terms as to embrace a corporation arbitrarily within a statutory reorganization which was not directly affected thereby, which had no voice in the planning of the reorganization, and which did nothing to make it effective. We suggest therefore that the acquisition by one corporation of the prescribed majority stock of another or of substantially all the properties of another corporation to amount to a statutory reorganization must be limited to the case of such an acquisition by one from the other. This must necessarily be the case where one corporation acquires substantially all the properties of another, because there is no way by which one corporation could acquire the properties of another except from that other. In the case of acquiring stock or acquiring property, the matter of ex-

change is involved, unless the transaction is solely on a money basis, the latter a situation with which we are not concerned in interpreting the statute. There is no good reason for supposing that it was the legislative intent that this element of a mutual exchange might be absent from the acquisition of stock when it must necessarily be present in the acquisition of property. The necessary limitation on the acquisition by one corporation of the property of another from that other in exchange for something going to that other corporation implies a similar limitation on the acquisition by one corporation of the prescribed majority of stock of another corporation to the case where it was acquired from that other corporation in exchange for something going to that other corporation. In short, before an acquisition by one corporation of the prescribed majority stock of another can amount to a reorganization, that stock must be transferred by the other corporation to the corporation acquiring it in exchange for securities or property of the acquiring corporation transferred to the other corporation or its nominees. Whether the corporation transferring the prescribed majority stock issues it from its treasury stock or secures it from its stockholders is of no significance. But the element of a mutual exchange is essential, for only out of the exchange arises the question of the recognition of a gain or loss to answer which paragraphs (2) and (3) of subdivision (b) of section 203 were prepared, but which in turn depend for clarity and definiteness upon the meaning of the term "reorganization", which in its turn is defined in subdivision (h).

The meaning which we suggest as the proper meaning of the parenthetical "acquisition" clause of clause (A) of subdivision (h) (1) is consistent with the main purpose of that subdivision, is consistent with the text of subdivision (h), with its position in that subdivision, with its parenthetical addition and with its introductory word "including". It avoids the inconsistency of having the necessary limitation on the acquisition of property differ from the limitation on the acquisition of the prescribed majority stock. Finally it avoids imputing to the Congress any intent to impose the arbitrary and inequitable consequences upon the taxpayer which must result from the interpretation suggested by the respondent.

Under the interpretation which we suggest, the acquisition of stock of the Koster Products Company by the B company from the A company would not amount to a statutory "reorganization" so far as the Koster Products Company was concerned. The Koster Products Company was not a party to that "acquisition", which concerned only the A company and the B company and the Koster Products Company was therefore not a party to any reorganization in 1924. The definition of "a party to a reorganization" as including both corporations in the case of the acquisition of the prescribed majority stock of another corporation was never intended to enlarge the meaning of the term "reorganization", or to declare corporations as parties to a reorganization when in fact there was no reorganization. All that Section 203 (h) (2) intended is that where the acquisition of stock or property occurs under circumstances within

the definition of a reorganization both the corporation acquiring and that transferring the stocks or property are to be deemed parties to the reorganization.

The Koster Products Company was not a party to the reorganization effected by the A company and the B company in 1924, and the stock of the Koster Products Company acquired by the B company from the A company in 1924, was like the other property acquired from the A company by the B company in 1924, entitled to the same basis for determining gain or loss that it had in the hands of the transferor—Sec. 204 (a) (7).

Appendix E

CORRECTED FIGURES FOR STATUTORY NET LOSS.

The B company claimed the loss in 1925 at \$846,461.85. In making that claim it had through error used as the cost figure of the property exchanged for the stock of the Koster Products Company the sum of \$910,701.85 (Ex. 4) and through error had set up \$64,240.00 as the amount received by the B company on the sale of this stock in 1925 (Ex. 4) instead of \$64,400.00. Exhibits 4, 6 and 7 show how the loss and the statutory net losses were figured as follows:

	<u>1925</u>	<u>1926</u>	<u>1927</u>
Cost	\$910,701.85		
Amount received	64,240.00		
Loss	846,461.85	\$504,502.66	\$306,348.56
Applied against income	341,889.19	198,154.10	110,486.33
Balance unapplied	504,572.66	306,348.56	195,862.23
Dividends	70.00		
	<hr/>	<hr/>	<hr/>
Statutory net loss	\$504,502.66	\$306,348.56	\$195,862.23

Correcting these figures and using the adjusted cost figures of \$738,374.21 which is the cost less depletion and depreciation and exclusive of carrying charges (Ex. 1, Trans. pp. 52, 53) the loss and the statutory net losses would be as follows:

	<u>1925</u>	<u>1926</u>	<u>1927</u>
Cost	\$738,374.21		
Amount received	64,400.00		
Loss	673,974.21	\$332,015.02	\$133,860.92
Applied against income	341,889.19	198,154.10	110,486.33
Balance unapplied	332,085.02	133,860.92	23,374.59
Dividends	70.00		
	<hr/>	<hr/>	<hr/>
Statutory net loss	\$332,015.02	\$133,860.92	\$ 23,374.59

The balance of statutory net loss of \$23,374.59 is the unextinguished balance remaining after applying the statutory net loss against 1927 income.

No. 7826

**In the United States Circuit Court of
Appeals for the Ninth Circuit**

CALIFORNIA BARREL COMPANY, INC., PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

**ON PETITION FOR REVIEW OF DECISION OF THE UNITED
STATES BOARD OF TAX APPEALS**

BRIEF FOR THE RESPONDENT

FRANK J. WIDEMAN,
Assistant Attorney General.

SEWALL KEY,
JOSEPH M. JONES,
Special Assistants to the Attorney General.

FILED

OCT 23 1935

PAUL A. O'NEILL

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OPINION BELOW

The only previous opinion in the present case is that of the United States Board of Tax Appeals (R. 18-23), which is not reported.

JURISDICTION

This appeal involves income taxes for the calendar year 1927 in the sum of \$14,915.65, and is taken from a decision of the Board of Tax Appeals entered November 8, 1934 (R. 24). The case is brought to this Court by petition for review filed January 29, 1935 (R. 24-36), pursuant to the pro-

visions of Sections 1001–1003 of the Revenue Act of 1926, c. 27, 44 Stat. 9, as amended by Section 1101 of the Revenue Act of 1932, c. 209, 47 Stat. 169.

QUESTION PRESENTED

Whether the petitioner corporation can utilize as a deduction in 1927 the net loss of its predecessor corporation in 1925 upon a showing that the business was the same and was reincorporated in order to comply with the local law.

STATUTE INVOLVED

Revenue Act of 1926, c. 27, 44 Stat. 9:

SEC. 206. * * *

(b) If, for any taxable year, it appears upon the production of evidence satisfactory to the Commissioner that any taxpayer has sustained a net loss, the amount thereof shall be allowed as a deduction in computing the net income of the taxpayer for the succeeding taxable year (hereinafter in this section called “second year”), and if such net loss is in excess of such net income (computed without such deduction), the amount of such excess shall be allowed as a deduction in computing the net income for the next succeeding taxable year (hereinafter in this section called “third year”); the deduction in all cases to be made under regulations prescribed by the Commissioner with the approval of the Secretary. (U. S. C. App., Title 26, Sec. 937.)

STATEMENT

The facts as stipulated (R. 39-51, and as found by the Board (R. 18-23), may be summarized as follows:

All three corporations involved in the transactions hereinafter set forth were organized under the laws of California for the purpose of engaging in the manufacture and sale of barrels.

California Barrel Company (hereinafter referred to as "A" company) was organized in 1906.

California Barrel Company, Inc. (hereinafter referred to as "B" company), was organized on February 15, 1924, for a term of fifty years, with a capital structure of 9,000 shares of voting preferred stock of \$100 par value each, and 9,000 shares of voting common stock of no par value, and on August 28, 1924, took over the business of "A" company.

On July 29, 1925, the Supreme Court of California in *Del Monte L. & P. Co. v. Jordan*, 196 Cal. 488, held that, pursuant to the State Constitution and Civil Code, the preferred and common shares of a California corporation must have the same par value. The Secretary of State thereupon refused to issue to "B" company the required statutory license to do business for the year 1926.

Under date of December 10, 1925, the "B" company sold certain assets transferred to it by "A" company (namely, stock of the Koster Products Company) at an alleged loss of \$846,461.85, result-

ing in an alleged net loss of \$504,572.66 for the taxable year 1925.

To provide a means for continuing the business during 1926, the "B" company caused to be organized on December 19, 1925, for a term of fifty years, the California Barrel Company, Inc. (hereinafter referred to as "C" company), the petitioner herein, which complied with the local law.

On December 31, 1925, all of "B" company's assets were transferred to "C" company. No steps were taken to dissolve the "B" company, and no decree of court dissolving the same has ever been entered.

In its return for the calendar year 1925, the "B" company reported a net loss of \$504,572.66. The "B" company filed no returns for the years 1926 and 1927. In its return filed for the calendar year 1927, the "C" company (petitioner herein) claimed a statutory net loss deduction in the amount of \$306,348.56 as a portion of the alleged net loss reported on "B" company's return for the year 1925. In determining the deficiency in controversy, the respondent disallowed such deduction on ground that the alleged net loss was not sustained by this petitioner. The Board approved this determination.

ARGUMENT

The power to tax income like that of the new corporation "C" is plain and extends to the gross income. Whether and to what extent deductions shall be allowed depends upon legislative grace;

and only as there is clear provision therefore can any particular deduction be allowed. It is submitted that the question involved in this appeal is controlled generally by *New Colonial Co. v. Helvering*, 292 U. S. 435, and specifically by *McLaughlin v. Purity Inv. Co.*, 75 F. (2d) 30 (C. C. A. 9th).

In *New Colonial Co. v. Helvering*, *supra*, the Supreme Court pointed out (p. 440):

The statutes pertaining to the determination of taxable income have proceeded generally on the principle that there shall be a computation of gains and losses on the basis of a distinct accounting for each taxable year; and only in exceptional situations, clearly defined, has there been provision for an allowance for losses suffered in an earlier year. Not only so, but the statutes have disclosed a general purpose to confine allowable losses to the taxpayer sustaining them, i. e., to treat them as personal to him and not transferable to or usable by another.

Obviously, therefore, a taxpayer seeking a deduction must be able to point to an applicable statute and show that he comes within its terms.

Section 206 (b) of the Revenue Act of 1926, *supra*, which governs the instant case, provides that a net loss of any taxpayer shall be allowed as a deduction in computing the net income "of the taxpayer" in the succeeding year. This provision is unambiguous. It has been held repeatedly that net losses are personal to the taxpayer and may be

applied only against the net income of the taxpayer in a succeeding year.

The question presented in the instant case is not in any essential particular different from that presented in *New Colonial Co. v. Helvering, supra*. Mr. Justice Van Devanter, in delivering the opinion of the Court, stated the question as follows (p. 437):

The question presented is: Where all the assets and business of an older corporation are taken over by a new corporation, specially organized for the purpose and having substantially the same capital structure, in exchange for a portion of its stock, which is distributed by the older corporation among the latter's stockholders share for share, thereby retiring the old shares, is the new corporation entitled, notwithstanding the change in corporate identity and ownership, to have its taxable income for the succeeding period computed and determined by deducting from its net income for that period the net losses sustained by the older corporation in the preceding period? * * *

In construing the pertinent section of the statute, the Court stated that (pp. 440-441):

Its words are plain and free from ambiguity. Taken according to their natural import they mean that the taxpayer who sustained the loss is the one to whom the deduction shall be allowed. Had there been a purpose to depart from the general policy in that regard, and to make the right to the

deduction transferable or available to others than the taxpayer who sustained the loss, it is but reasonable to believe that purpose would have been clearly expressed. And as the section contains nothing which even approaches such an expression, it must be taken as not intended to make such a departure.

There, as here, the taxpayer contended that even though the section was not literally complied with, for all practical purposes the new corporation was the same entity as the old one and therefor the same taxpayer. The Court, in answer to this argument, stated that the case involved no such exceptional circumstances as to warrant the disregard of the separate entity of the corporation. On the contrary, the Court was of the opinion that the case was a typical one for the application of the separate entity rule, and concluded that the alternative contention had no legal basis.

In *McLaughlin v. Purity Inv. Co.*, *supra*, this Court applied the principles enunciated in *New Colonial Co. v. Helvering*, *supra*, to a set of facts substantially identical with the case at bar. There, as here, the predecessor corporation was formed under the laws of California, with preferred stock having par value and common stock having non-par value. Following the decision of the Supreme Court of the State of California in *Del Monte L. & P. Co. v. Jordan*, *supra*, the Commissioner of Corporations denied the corporation a license to

transact business, as was the situation in the case at bar. Thereupon, a new corporation was formed with a substantially identical stock structure to take over the assets and business of the predecessor corporation. The only difference between the two cases was that in the *Purity Inv. Co.* case the new corporation was chartered under the laws of Nevada instead of California. But this factual distinction clearly had no legal effect on the question involved. After quoting at length from the opinion of the Supreme Court in *New Colonial Co. v. Helvering*, *supra*, this Court said (p. 33):

There is no fact in the instant case which takes it out of the rule laid down by the Supreme Court in the *New Colonial Ice Company Case*. The mere fact the predecessor California corporation was but a *de facto* corporation would not affect the situation. As such *de facto* corporation, it was entitled to enjoy the privileges of a corporation until action was brought by the Attorney General for dissolution. It had the power to convey, and did convey, its assets to another corporation organized for such purpose. Even though it was deemed desirable to have a stock structure with both par and non-par stock, and this could be accomplished only by a corporation organized in pursuance of the laws of another state, such corporation of necessity would be regarded "as a distinct corporate entity and therefore free from difficulties attending the old one." * * *

Thus, although its charter was defective, the predecessor corporation in the case at bar was a *de facto* corporation, a separate business unit within the contemplation of the law.

The alternative contention of the taxpayer, that the new corporation was substantially the same taxpayer as the predecessor corporation by reason of the identity of interest and continuity of business, was further met in the recent case of *Turner-Farber-Love Co. v. Helvering*, 68 F. (2d) 416 (App. D. C.), where the court, after concluding that the tax laws treat separate corporations as separate taxpayers and that the statute governing deductions confines the use of the loss to the taxpayer who sustains it, made this pertinent statement (p. 417):

Nor is the situation in this respect changed because in the transfer of assets from the one company to the other a continuing business is involved. The fact of separate identity still remains, and the rule that courts will look beyond the shadow to the substance, which petitioner invokes, is here no more applicable than it was in *New York, etc., R. Co. v. Burnet*, 62 App. D. C. 29, 64 F. (2d) 152, 154, where we said it is applied only in cases in which to refuse to apply it would be to countenance fraud.

In view of the premises, it is submitted that this Court could well agree with the conclusion reached by the Circuit Court of Appeals for the First Circuit in the closely related case of *Athol Mfg. Co. v.*

Commissioner, 54 F. (2d) 230, where the following conclusion was reached (p. 231):

We fail to see how we can add anything to what was stated by the Board of Tax Appeals in its opinion. We are in full accord with its ruling and finding that the petitioner was an independent entity from the old corporation whose assets and business it took over; that the losses sustained by the old company in conducting its business during 1922 and a part of 1923 were not the petitioner's losses; and that it was not entitled to deduct the same in its tax return.
* * * We can hardly see why this appeal was taken.

CONCLUSION

Since the petitioner corporation is not the same taxpayer as the predecessor corporation, it is not entitled to a deduction in 1927 for any portion of a net loss sustained in 1925 by its predecessor. The judgment of the Board of Tax Appeals is correct and should be affirmed.

Respectfully submitted.

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Assistant Attorney General.

SEWALL KEY,
JOSEPH M. JONES,

Special Assistants to the Attorney General.

OCTOBER 1935.

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United States
Circuit Court of Appeals
For the Ninth Circuit.

JOHN P. McLAUGHLIN, as United States Collector
of Internal Revenue, First District of California,
Appellant,

vs.

COOS BAY LUMBER COMPANY, a corporation,
Appellee.

Transcript of Record

Upon Appeal from the District Court of the United
States for the Northern District of California,
Southern Division.

FILED

MAY 25 1935

PAUL P. O'BRIEN,

CLERK

United States
Circuit Court of Appeals

For the Ninth Circuit.

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Appellee.

Transcript of Record

Upon Appeal from the District Court of the United
States for the Northern District of California,
Southern Division.

INDEX.

[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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NAMES AND ADDRESSES OF ATTORNEYS.

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P. O. Bldg., San Francisco, Calif.,
Attorneys for Defendant and Appellant.

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414 Merchants Exchange Bldg., San Francisco,
California,
Attorneys for Plaintiff and Appellee.

In the Southern Division of the District Court of the
United States, in and for the Northern District of
California.

At Law.
No. 19268K.

COOS BAY LUMBER COMPANY, a corporation,
Plaintiff,

vs.

JOHN P. McLAUGHLIN, as United States Collector
of Internal Revenue, First District of California,
Defendant.

COMPLAINT FOR RECOVERY OF TAXES
ERRONEOUSLY PAID.

Now comes the plaintiff above named and files this
its Complaint against the defendant above named and
for cause of action alleges:

I.

That the plaintiff above named now is, and at all
times herein mentioned was, a corporation organized

and existing under and by virtue of the laws of the State of Delaware and having its executive offices and its principal place of business in the State of California in the City and County of San Francisco. That the plaintiff was formerly named the Pacific States Lumber Company, which name was duly changed to the Coos Bay Lumber Company on or about February 15th, 1928.

II.

That at all times herein mentioned, and at the time of the purchase of the stamps and the payment of the tax hereinafter described, defendant John P. McLaughlin was the duly appointed, acting and qualified United States Collector of Internal Revenue for the First District of California, having his official place of business in the City and County of San Francisco, State and Northern District of California. [1*]

III.

That on or about the 18th day of September, 1925, the plaintiff had duly issued and outstanding its first mortgage bonds in the principal amount of upwards of \$7,000,000; that the plaintiff was in default in the payment of principal and interest on said bonds on said September 18th, 1925.

IV.

That there was organized during the month of September, 1925, the bondholders' protective committee for holders of said bonds of the plaintiff, and that under an agreement dated September 18th, 1925, between said bondholders' protective committee and bondholders of the Pacific States Lumber Company, a copy of which

*Page numbering appearing at the foot of page of original certified Transcript of Record.

agreement is attached hereto, marked Exhibit "A" and hereby made a part hereof, bonds of the plaintiff were deposited with said committee for the purposes set forth in said Exhibit "A".

V.

That said bondholders' committee, acting pursuant to the authority conferred upon it in said deposit agreement, on the 19th day of April, 1927, outlined a plan of reorganization of the plaintiff, whereby bonds acquired by the committee should be exchanged for first preferred stock of the plaintiff of the principal par value to the principal par value of the bonds held by the committee, together with one share of no par common stock of the plaintiff for each \$100 principal par value of the bonds surrendered; that the plan provided not that the bondholders' committee should receive the issue of stock from the plaintiff, but that the stock should be issued directly and held only by voting trustees named by the bondholders' protective committee, pursuant to said plan. That the pertinent portions of said plan are as follows:

"Pacific States Lumber Company
Plan and Agreement of Reorganization
Adopted by the Bondholders Protective Committee
April 19, 1927.

1. RECAPITALIZATION. All the present stock of Pacific States Lumber Company shall be cancelled, and the Company recapitalized upon the following basis: [2]

\$6,827,700 First Preferred Stock, entitled to dividends at 7%, cumulative from July 1, 1925, redeemable at 105 and accumulated dividends.

\$1,000,000 Second Preferred Stock, entitled to dividends at 6% from and after January 1, 1932, redeemable at par and accumulated dividends, if any.

68,277 shares of No Par Value Common Stock.

Common Stock only shall have voting power, but no dividends shall be paid on Common Stock until January 1, 1933, nor thereafter until all accumulated dividends on Preferred Stocks have been paid, and suitable sinking fund provision made for the retirement of Preferred Stocks in the order of their preference as the property is depleted by the liquidation of assets.

2. STOCK DISTRIBUTION. For each \$100 principal of the present \$6,827,700 of bonds outstanding, there shall be issued in exchange \$100 par value of First Preferred Stock and one share of Common Stock. Any of the authorized First Preferred and Common Stock not so exchanged shall be cancelled.

All of the Second Preferred Stock shall be issued to a Trustee for the former stockholders of all classes to be divided in such proportion as they shall determine.

3. VOTING TRUST. The First Preferred and Common Stock shall be held and voted by a committee of five Voting Trustees, for the benefit of the owners thereof, with discretionary power to sell all of the Common and/or First Preferred Stock as a unit, but upon terms which will retire or purchase all of the First Preferred Stock at not less than par and accumulated dividends, unless and except otherwise authorized or instructed in writ-

ing by not less than 75% in interest of the First Preferred Stockholders. Also all the assets of the Company may be sold or mortgaged upon majority vote of the Common Stock.”

VI.

That the plaintiff in the month of September, 1927, agreed to carry out this plan; that before its consummation, the number of bonds outstanding was reduced to the principal par value of \$6,375,700;

That on January 27th, 1928, the bondholders’ committee adopted the following resolution:

“RESOLVED FURTHER: That the Company be, and hereby is, requested to complete its corporate reorganization in accordance with the said Plan, and to issue 63,757 shares of first preferred and a corresponding number of no par value common stock to the Trustees to be named pursuant to Section 3 of said Plan.” [3]

That the said resolution was placed upon the minutes of the meeting of the Directors of the plaintiff company held in San Francisco on the 27th day of January, 1928, and the following resolution was passed by the Directors:

“RESOLVED that the minutes of the Bondholders’ Protective Committee, as read by Mr. Arnold, be spread on the minutes of the Company and that the Officers of the Company be empowered and instructed to carry out all of acts provided therein, to be performed by the Company.”

VII.

That thereafter, the plaintiff proceeded to, and did, amend its Certificate of Incorporation to authorize the issue of the stock in accordance with the plan of reorganization.

VIII.

That on or about the 25th day of February, 1928, plaintiff did issue 63,757 shares of first preferred stock and 63,757 shares of no par common stock to G. S. Arnold, C. T. MacNeille, N. V. Wagner, A. McC. Washburn and Homer W. Bunker, being the persons theretofore named by the bondholders' protective committee as the trustees to whom said stock should be issued, in accordance with the said plan of reorganization, said persons being the same persons who then comprised said bondholders' protective committee; that said shares were issued, as aforesaid, in two certificates, one certificate for 63,757 shares of first preferred stock, and one certificate for 63,757 shares of no par common stock;

That at the same time, the plaintiff did issue to one F. A. Warner, as trustee for the former stockholders of the plaintiff, 10,000 shares of second preferred stock, in accordance with said plan of reorganization, said 10,000 shares of second preferred stock being issued in one certificate.

IX.

That said trustees did receive said stock and hold said stock as an original issue of said stock to them, and not by transfer in any wise from any persons whomsoever; that they held said stock under the terms of a trust agree- [4] ment between said trustees and said

bondholders' protective committee, which trust agreement is attached hereto, marked Exhibit "B" and hereby made a part hereof.

X.

That on or about February 25th, 1928, said plaintiff did purchase from the Government of the United States and defendant John P. McLaughlin, the Collector of Internal Revenue at San Francisco, Internal Revenue stamps in the amount of \$4,962.99; that said plaintiff, upon the issue of said 63,757 shares of first preferred stock and 63,757 shares of no par common stock to said trustees, as aforesaid, and said 10,000 shares of second preferred stock to the trustee, as aforesaid, did affix to the certificate stubs therefor said \$4,962.99 Internal Revenue stamps as follows:

To the issue of first preferred stock	\$3,187.85
To the issue of no par common stock	1,275.14
and to the issue of second preferred stock	500.00
	<hr/>
	\$4,962.99.

XI.

That said common stock without par value had at the time of said issue no actual value whatsoever and, hence, the whole issue thereof required but a one cent Internal Revenue stamp be affixed and cancelled, and hence Internal Revenue stamps in the amount of \$1,275.13 were erroneously affixed to this issue of no par common stock; that said issue of second preferred stock was merely the exchange of one kind of stock for another, without thereby increasing the capital of the

plaintiff, and was therefore not an original issue of stock and did not require any Internal Revenue stamps whatsoever to be affixed and cancelled, and hence Revenue stamps in the amount of \$500.00 were erroneously affixed to the issue of second preferred stock.

XII.

That on or about December 17th, 1928, the plaintiff, on forms made and [5] provided for such cases, duly filed with the Collector of Internal Revenue, at San Francisco, California, its claim for refund in the sum of \$1775.13, together with interest thereon, as allowed by law; that this claim for refund claimed recovery of the amount of stamps erroneously affixed to the issue of said no par common stock in the amount of \$1275.13, and the amount of \$500.00 for stamps affixed to said issue of second preferred stock.

XIII.

That the then Commissioner of Internal Revenue, Robert H. Lucas, on or about March 3rd, 1930, in his letter of that date addressed to the plaintiff, a copy of which letter is attached hereto, marked Exhibit "C" and hereby made a part hereof, did allow and find in favor of plaintiff on its claim for refund in the sum of \$1775.13 for the reason (1) that the second preferred stock issued in exchange for the outstanding shares did not involve an increase in the capital of the corporation and was not an original issue of stock within the meaning and provisions of Section 800, Schedule A-(2), of the Revenue Act of 1926, but was merely the exchange

of one kind of stock for another and, therefore, documentary stamps of the value of \$500 were erroneously affixed on this issue; and for the reason that (2) the common stock without par value had no actual value at the time of issue and, therefore, documentary stamps of the value of \$1275.13 were erroneously affixed on this issue.

XIV.

That Robert H. Lucas, as Commissioner of Internal Revenue, in said letter of March 3rd, 1930, did erroneously claim that Internal Revenue stamps to the extent of \$2,550.28 should have been affixed or paid upon an alleged transfer to the said voting trustees by the former bondholders or the bondholders' protective committee of an alleged right in them to receive the said 63,757 shares of first preferred stock and 63,757 shares of common stock without par value; that this claim of the Commissioner was unfounded and erroneous since there never existed such right in the former bondholders or the bond- [6] holders' protective committee to receive said stock, and hence there could be no transfer thereof; that the Commissioner, in said letter, did also determine, which determination the plaintiff does not contest, that Internal Revenue stamps in the amount of \$200 should have been affixed to the transfer to said Warner as trustee of the right of the stockholders of the plaintiff to receive said 10,000 shares of second preferred stock.

XV.

That on or about the 15th day of July, 1930, the plaintiff was notified of an assessment against it in the

amount of \$975.15, being the difference between the credit of \$1,775.13 for Internal Revenue stamps found by the Commissioner to have been erroneously affixed to said issue of no par common stock and second preferred stock as aforesaid, and \$2750.28, which \$2750.28 is the sum of \$2550.28, being the amount erroneously claimed by the Commissioner of Internal Revenue in said letter of March 3rd, 1930 to have been due in Internal Revenue stamps upon the transfer to the voting trustees by the former bondholders or the bondholders' protective committee of an alleged right to receive said issue of first preferred and no par common stock, as aforesaid, and \$200 being the amount claimed by the Commissioner of Internal Revenue as due upon an alleged transfer of a right of the former stock holders to receive the issue of said preferred stock, as aforesaid; that on or about July 27th, 1930, the plaintiff duly filed with the defendant Collector of Internal Revenue for the First District of California at San Francisco, on forms made and provided for such cases its claim for abatement of this assessment of \$975.15; that this claim in abatement was rejected on or about January 27th, 1931, by R. M. Estes, Deputy Commissioner of Internal Revenue, and that this assessment of \$975.15 and \$64.76 interest thereon—\$1,039.91 in all—was paid on February 11th, 1931, by the plaintiff to defendant John P. McLaughlin, the Collector of Internal Revenue at San Francisco, California. [7]

XVI.

That on or about the 24th day of February, 1932, the plaintiff, on forms made and provided for such cases,

duly filed with the defendant Collector of Internal Revenue for the First District of California, at San Francisco, California, its claim for refund in the amount of \$2,615.04, together with interest thereon as allowed by law, being said sum of \$1,039.91 and the credit of \$1,775.13 less the \$200 claimed by the Commissioner of Internal Revenue as due upon an alleged transfer of the right of the former stockholders of the plaintiff to receive the issue of second preferred stock as aforesaid, which determination the plaintiff does not contest; that this claim for refund was filed within four years of the purchase of the said Internal Revenue stamps by the plaintiff from the defendant and within four years of the payment of the aforesaid assessment against the plaintiff and that this claim for refund was upon the same grounds herein alleged; that this claim for refund was rejected and disallowed by the Commissioner of Internal Revenue, David Burnet, on or about May 3rd, 1932.

XVII.

That all of said \$2,615.04, represented by \$1,575.13 in documentary Internal Revenue stamps erroneously affixed and cancelled and the \$1,039.91 paid by the plaintiff to the defendant on or about February 11th, 1931, as aforesaid, was erroneously paid, assessed and collected, and is now unpaid, due and owing to the plaintiff from the defendant.

XVIII.

That this case arises under the laws of the United States providing for Internal Revenue, and is within the jurisdiction of this Honorable Court.

WHEREFORE, plaintiff prays for judgment against the defendant in the amount of \$2,615.04, together with interest thereon as allowed by law, and for its costs of suit herein, together with such other and further relief as may in the premises seem meet.

WILLIAM DENMAN,
Attorney for Plaintiff. [8]

State of California,
City and County of San Francisco—ss.

H. W. BUNKER, being first duly sworn, deposes and says:

That he is the President of the Coos Bay Lumber Company, a corporation, the plaintiff named in the foregoing Complaint, and as such officer is duly authorized to make this verification for and in behalf of said corporation.

That he has read the said Complaint and knows the contents thereof; that the same is true of his own knowledge, except as to the matters therein stated on information or belief, and as to those matters he believes it to be true.

H. W. BUNKER.

Subscribed and sworn to before me, this 28th day of June, A. D. 1932.

[Seal] KATHRYN E. STONE,
Notary Public, in and for the City and County of San Francisco, State of California. [9]

EXHIBIT "A".

AGREEMENT BETWEEN BONDHOLDERS OF
PACIFIC STATES LUMBER COMPANY AND
THE BONDHOLDERS PROTECTIVE COM-
MITTEE, REPRESENTING THE HOLDERS
OF FIRST MORTGAGE EIGHT PER CENT
GOLD BONDS, DATED SEPTEMBER 18, 1925.

AGREEMENT, Dated September 18th, 1925, between such holders of the following described Bonds of the PACIFIC STATES LUMBER COMPANY (herein called the Company:)

First Mortgage Eight Per Cent Gold Bonds issued under the First Mortgage by the Company to Central Trust Company of Illinois, and the Michigan Trust Company, Trustees, dated January 1, 1922 and the unpaid and past due coupons hereinafter mentioned (herein called, collectively, the Bonds);

who shall become parties hereto by signing this agreement or depositing their Bonds hereunder, or both (herein called Depositors) parties of the first part, and G. S. Arnold, Attorney, of San Francisco, California, C. T. MacNeille, of Halsey, Stuart & Co., Chicago, Illinois, N. V. Wagner, of Second Ward Securities Co., Milwaukee, Wisconsin, Alexander V. Ostrom, Representing Wells-Dickey Co., of Minneapolis, Minnesota, and Homer W. Bunker, of Peirce, Fair & Co., San Francisco, California (herein called the Committee), parties of the second part.

Whereas, the Company has outstanding the following funded debt:

First Mortgage Bonds (interest July 1 and January 1) Seven Million Seven Hundred and Four Thousand Dollars (\$7,704,000) together with past due and unpaid coupons on the First Mortgage Bonds of the Company maturing July 1, 1924, and January 1, 1925, in the aggregate amount of five hundred seventy-three thousand and forty dollars (\$573,040); and

Whereas, the Company in common with other fir lumber manufacturers generally, has, during and since the year 1924, suffered from conditions of overproduction in the lumber industry on the west coast of the United States, and from consequent fir lumber market depression, so that during said period it did not make from revenue a sufficient sum to pay its fixed charges; and

Whereas, by reason thereof there exists a grave condition affecting the common interest of the Bondholders; and

Whereas, in view of the whole situation, and in order, if possible, to avoid receivership and foreclosure and the disturbance, expense and loss attendant thereon, it is obvious that the Bondholders should have concerted representation that can be constantly advised of all developments and able accurately to judge of the best course for all, and should unite for the protection and promotion of their common interests;

NOW, THEREFORE, THIS AGREEMENT WITNESSETH: That in consideration of the premises, of the advantages which may accrue from the union of common interest and concert of action and of the mutual provisions and stipulations herein contained, the Deposi-

tors, each for himself and not for any of the others, do agree with each other and with the Committee, as follows:

First. The Depositors hereby make, constitute and appoint G. S. Arnold, C. T. MacNeille, N. V. Wagner, Alexander V. Ostrom, Homer W. Bunker, and their successors a Committee under this agreement with all the rights, privileges and powers herein delineated.

Each of the Depositors agrees to, and hereby does, deposit with one of the Depositaries to be hereafter named, the number of Bonds owned by him with coupons maturing January 1, 1926, or on such later date as may be designated by the Committee together with all coupons subsequently maturing in order that said Bonds may be held subject to the order of the Committee under this agreement. The Committee may in its discretion and upon such terms and conditions as it may in each instance prescribe, permit the deposit hereunder of Bonds without such coupons, or of coupons without Bonds. The term "Bonds" whenever used herein shall be deemed to include all coupons thereon maturing on and after January 1, 1926, or on such later date as may be designated by the Committee as well as coupons which have matured prior to the date hereof and are past due obligations of the Company, unless such meaning is plainly inconsistent with the context. The title to all of said Bonds is, for the period hereinafter named, vested in the Committee to hold the same for the purposes herein set forth and to have and exercise, with respect thereto, all rights and powers of every kind and description given by law or by the terms of the Bonds or in any instrument securing the same, which the Depositors might thus have had or exercised

in respect to the Bonds so deposited or the property upon which the same are secured.

For all Bonds deposited negotiable receipts in a form approved by the Committee shall be issued by the Depositary receiving the same and any bondholders so depositing the same and accepting such receipts and all transferees thereof shall be as fully bound by and be parties to this agreement as if they had signed the same. The Committee shall make suitable rules and regulations for the record both of original issue and transfer of these certificates. The registered holders of the respective certificates of deposit may be considered and treated as the absolute owners thereof and of all of the rights of the original Depositors and neither the Committee nor any member of it nor the Depositary shall be affected by any notice to the contrary.

Separate copies of this agreement may be signed by different members of the Committee or Depositors with the same effect as if all signatures had been appended to one instrument.

Second. Four-fifths of the Committee, as at any time constituted, shall have and exercise all the powers hereby conferred upon the Committee and may exercise such powers either in meeting or in writing, or by telegram without a meeting. Any member may vote or act by proxy who may, but need not, be another member, or by alternate. The Committee may limit or extend the time within which such deposits may be made hereunder, fix conditions or penalties under which such are made and, either generally or in special instances, in its discretion, accept deposits after the time has expired, or waive such conditions or penalties. Subject

to the provisions hereof, the Committee may fix its rules of action or procedure, elect such officers as the Committee may deem necessary, who may or may not be members of the Committee, select, employ and remove Depositaries, counsel, accountants, experts, agents and employees and fix the compensation of all thereof and its own reasonable compensation, if any, and generally may make or authorize such other expenditures as it shall deem necessary or appropriate for the purposes of this agreement.

It may, from time to time, add to its number, fill vacancies therein, however caused, if it deem advisable that such vacancies be filled, but four-fifths of the Committee, as at any time constituted, shall have and exercise all powers herein conferred.

No member, officer, agent, employee, or other representative of the Committee shall be disqualified to perform such function solely because he may be the holder of any security of any class, including stock, nor because of any relation he may directly or indirectly bear to the Company, its property, security or instrument securing the same.

To meet conditions not now foreseen or as they may vary, the Committee may, if its judgment so require, amend this agreement by filing the amendment with the then Depositaries, if any, and/or by giving the notice specified in paragraph Sixth. Any Depositor may, within twenty (20) days after the first publication, withdraw herefrom and, having discharged all then existing obligations under the agreement, including his pro rata part of any amount due under paragraph Fourth, be relieved from further obligation and divested of all rights hereunder. Any Depositor not so with-

drawing shall be deemed to have consented to such amendment.

Third. The Committee shall have power and authority, in its name, as owner of the deposited Bonds or otherwise, to take all such actions and steps as it shall deem advisable, for protecting, securing, supporting or subserving the true and ultimate rights of the holders of the deposited Bonds as fully as said holders themselves might do had the Bonds not been deposited or assigned; including, without intending, however, to limit, the general authority granted, among other things, the right to institute and prosecute any proceedings at law or in equity, intervene in, compromise or discontinue such proceedings and generally apply for any remedy, procedure or judicial act therein; to waive or suspend any default in the bonds or coupons deposited hereunder; either collect and receive any payments on account of the principal or interest of the deposited Bonds and distribute the same among the holders of negotiable receipts representing the same, or cause such payments to be made directly to such holders without preference or priority of one holder over another or of one receipt over another receipt; to vote at any meeting of the Bondholders under any instrument securing the same; in its own uncontrolled discretion, demand, request or require the trustee or trustees under any instrument securing any of the deposited Bonds, to take or refrain from taking any action which the Bondholders, either as individuals or in conjunction with other holders, could take; generally to exercise, or refrain from exercising, as in the Committee's discretion it conceives to be for the common interest of all the Depositors of any one class any

election, prerogative, voting or other right or function that all the holders of the deposited Bonds could have or perform under the instrument securing the same; may furnish any trustee with any security or evidence which it may require and generally do and perform all acts and requests which the Committee may deem advisable to the accomplishment of this agreement as fully as if the Committee were the absolute and unrestricted holders and owners of the deposited Bonds. The power to exercise any revocable act or function includes the right to revoke or withdraw the same.

So long as no default shall occur under the terms of the mortgage, or when a default shall have occurred under the terms of the mortgage and such default has been waived, then and in each and every such event notwithstanding anything herein contained, the Committee shall, at the request and direction of any Depositor, tender bonds represented by any receipt held by such Depositor to the Company or the Trustee or Trustees under said Mortgage, or its or their authorized agent, and shall upon the acceptance of such tender, or upon call duly made by the Company, or said Trustee or Trustees, deliver the bonds so tendered or so called to the Company or said Trustee or Trustees, or its or their authorized agent, receive the proceeds thereof and distribute to the holder or holders of the receipts representing such bonds the proceeds thereof, after deducting pro rata the expenses, expenditures and compensations provided in Section Fourth hereof.

The Committee shall have power and authority, if and when in its judgment it becomes advisable so to do, but not otherwise, to propose or adopt a plan and

agreement of reorganization providing for the appointment of Managers thereof, who may but need not be members of the Committee, and vesting in such Managers power and authority to do and perform all acts in relation to any reorganization or sale of any securities that the Committee may deem advisable or expedient to be possessed by such Managers to carry out the plan so prepared and adopted. The power to adopt or approve such plan shall include the power from time to time to amend the same in such manner upon such notice and with such right of withdrawal as may therein be provided.

Upon the adoption or approval of such plan a copy thereof shall be filed with each Depositary. Notice of the fact of approval, adoption and filing shall be published as provided in paragraph Sixth and as nearly contemporaneously as practical with the first publication a copy of the plan shall be mailed to each Depositor at the address shown on the books of the Depositaries. Any Depositor may within twenty (20) days from the date of the first publication of such notice, withdraw herefrom upon the same conditions and with like effect as is provided in paragraph Second in case of amendment. Any Depositor not so withdrawing shall be deemed to have assented to such plan.

Fourth. For all expenses, expenditures or compensations incurred by the Committee in the discharge of its duties, it shall have a lien on the deposited Bonds, proceeds or income therefrom, not, however, to exceed an amount in aggregate equal to five per cent of the face of such deposited Bonds. For the payment of such obligations, the Committee may procure advancements and, subject to the above limitation as to amount, secure their payment by like lien.

Fifth. The Depositaries to be named will be the agents of the Committee, and it shall have power to remove them, increase or decrease their numbers and make rules regulating their functions and authorities. The Depositaries and their agents shall be bound only to exercise reasonable care in the safekeeping of the deposited Bonds or other securities or property deposited with them hereunder and to deal therewith in accordance with the directions of the Committee; and the directions of the Committee shall be a complete justification for any action or omission to act of the Depositaries and their agents. The Depositaries or any or either of them may resign upon thirty days' notice in writing to the Committee or such shorter notice as the Committee may accept. The Committee may fill any vacancy arising in the office of a Depositary.

Meetings of Depositors may be called at any time by the Committee by notice mailed to them at the address shown on the books of the Depositaries, and such notice shall be deemed personal; notice as in paragraph Sixth shall also be given. The Committee shall have power to adopt rules for the regulation of such meetings and for the determination of the ownership of such certificates for the purpose of voting, including the power of voting by proxy.

This agreement shall terminate on September 18, 1928, and may be terminated at any time prior thereto or prior to the date of any extension hereof made as herein provided by the Committee in its discretion by giving the notice specified in paragraph Sixth hereof, in either of which cases the deposited bonds shall be returned to the holders of the certificates of deposit upon surrender thereof in negotiable form under such

rules of identification as the Committee may adopt and after payment of all obligations owed to or by the Committee as provided in paragraph Second hereof.

This agreement may be extended from time to time for periods not exceeding in the aggregate three years from September 18, 1928, by amendments hereof made in the manner and with the effect provided in paragraph Second hereof. At any time and for any reason, anything herein to the contrary notwithstanding, the holders of a majority or more in amount of the Bonds then deposited hereunder may withdraw herefrom in the manner and with the effect prescribed in the last paragraph of Section Second for the withdrawal herefrom in the event of an amendment of this agreement. In such event the Committee may, subject to discharge of such obligations, return all Bonds yet remaining hereunder and declare this agreement ended.

No member of the Committee shall be liable for any errors of judgment nor, in any event, for the acts or omissions of any other member of the Committee or of any agent, representative or employee of the Committee nor of any Depositary, nor for anything save his own willful misconduct.

Sixth. Hereinbefore there are several references to notices as specified in this Section Sixth. Wherever such reference is made it is intended that such notice shall be given by mailing to the Depositors at the addresses shown on the books of the Depositaries, and, after date of mailing, by publication thereof twice a week for two successive weeks in newspapers of general circulation, one each of the cities of New York, Chicago, Milwaukee, Minneapolis and San Francisco, and the date of the first publication shall be deemed the date of the notice.

Seventh. An original counterpart of this agreement shall be signed by all the members of the Committee and filed with the Secretary of the Committee. By receiving a certificate of deposit executed by or on behalf of a Depositary, any recipient or holder thereof shall thereby become and be a party to this agreement and be bound by its provisions with the same force and effect as though actually executing and delivering the same. The Committee shall, under no circumstances, be under any obligation, legal or equitable, expressed or implied, to any person whomsoever other than the holders of certificates of deposit issued hereunder.

G. S. ARNOLD,
C. T. MACNEILLE,
N. V. WAGNER,
ALEXANDER V. OSTROM,
HOMER W. BUNKER.

Depositor.

Address.

The following Depositaries have been appointed by the Committee pursuant to the foregoing Agreement:

Central Trust Company of Illinois,
125 West Monroe street, Chicago, Illinois;
Second Ward Savings Bank,
Third, West Water and Cedar streets, Milwaukee, Wisconsin;
Minneapolis Trust Company,
115 South Fifth street, Minneapolis, Minnesota;
Bank of California, N. A.,
400 California street, San Francisco, California.

EXHIBIT "B"

STOCK TRUST AGREEMENT OF COOS BAY
LUMBER COMPANY, DATED

FEBRUARY 23, 1928

THIS AGREEMENT, made this twenty-third day of February, 1928, by and between G. S. ARNOLD, C. T. MacNEILLE, N. V. WAGNER, A. McC. WASHBURN, and HOMER W. BUNKER, constituting the Pacific States Lumber Company Bondholders' Protective Committee and the Managers of the Plan of Reorganization of said company and hereinafter called the "Committee," parties of the first part, and G. S. ARNOLD, C. T. MacNEILLE, N. V. WAGNER, A. McC. WASHBURN, and HOMER W. BUNKER, hereinafter called the "Trustees," parties of the second part,
WITNESSETH:

Whereas, the Committee has caused to be delivered to said trustees, certificates representing 63,757 shares of the first preferred stock and an equal number of shares of no par value common stock of Coos Bay Lumber Company (formerly Pacific States Lumber Company) to be held by said trustees for and on behalf of the beneficial owners thereof as designated by the Committee.

NOW, THEREFORE, IT IS AGREED AS FOLLOWS:

1. The Trustees shall issue trust receipts and cause the same to be delivered to said beneficial owners, the form thereof to be substantially as follows:

“No. Units

COOS BAY LUMBER COMPANY

First Preferred and Common Stock Trust Receipt.

This Certifies that as hereinafter provided and on surrender thereof..... will be entitled (out of certificates hitherto delivered to the undersigned trustees under the agreement hereinafter mentioned) to receive certificates for shares of 7% first preferred stock with dividends cumulative from July 1, 1925 and for an equal number of shares of no par value common stock of Coos Bay Lumber Company (formerly Pacific States Lumber Company) and to receive payments equal to any dividends which may be collected by the Trustees upon such shares of stock received and held by the Trustees under said agreement.

This receipt is issued pursuant and subject to an agreement dated February 23, 1928 and executed by and between G. S. Arnold, C. T. MacNeille, N. V. Wagner, A. MacC. Washburn, and Homer W. Bunker, as the Pacific States Lumber Company Bondholders' Protective Committee, parties of the first part, and G. S. Arnold, C. T. MacNeille, N. V. Wagner, A. McC. Washburn, and Homer W. Bunker, Trustees, parties of the second part, defining all rights of the holders hereof and the duties and liabilities of the Trustees hereto subscribed, a copy of which is deposited with Central Trust Company of Illinois, Depositary, and Transfer Agent, and reference to which is hereby made for a more

particular description of the rights of the holder hereof. The stock herein described shall be deliverable to the holder hereof upon the written demand of not less than 75% in interest of the first preferred stock represented by receipts of which this receipt is one, and in any event, not later than January 1, 1932.

All first preferred and/or common stock in the hands of the Trustees may be sold as a unit but upon terms which will retire or purchase all of the first preferred stock at not less than par and accumulated dividends unless and except otherwise authorized or instructed in writing by not less than 75% in interest of the first preferred stockholders as represented by the trust receipts issued therefor.

This trust receipt is transferable on the books of the Trustees or their agents on surrender hereof by the registered holder or by attorney duly authorized; and until so transferred, the Trustees may treat the registered holder as the owner of this trust receipt for all purposes whatsoever. In the event of transfer, new trust receipt or receipts of like tenor herewith shall be issued in lieu hereof, provided that each trust receipt so issued shall be in units representing an equal number of shares of said first preferred and common stock.

This trust receipt is not valid unless signed on behalf of the Trustees by Central Trust Company

of Illinois, their duly authorized transfer agent.

G. S. ARNOLD,

C. T. MacNEILLE,

N. V. WAGNER,

A. McC. WASHBURN,

HOMER W. BUNKER,

Trustees.

By CENTRAL TRUST COMPANY
OF ILLINOIS,

Depository and Transfer Agent.

By

Assistant Secretary.

For value received I hereby sell, assign and
transfer unto

units represented by this trust receipt and do
hereby irrevocably constitute and appoint.....

.....attorney to transfer
said units on the books of the Depository and
Transfer Agent, with full power of substitution.

..... (Seal)

In Presence of:

.....
Dated ”

The said trust receipts shall be transferable only on
the books of the Depository and Transfer Agent on
surrender thereof by the holder or by attorney duly
authorized and in accordance with rules from time to
time established for that purpose by the Trustees and
until so transferred, the Trustees may treat the regis-

tered holders as shown by said books as the owners of said trust receipts for all purposes whatsoever. The Trustees may cause the transfer books to be closed at any time for the holding of meetings or the payment of dividends or for any other purposes. All transfers shall be made by units and each unit shall represent one share of such first preferred stock and one share of common stock.

2. Unless otherwise terminated as hereinafter provided, this agreement shall remain in effect until but shall terminate upon January 1, 1932. This agreement may be terminated at any time by the written demand served upon the Trustees, or their authorized agent, of not less than 75 per cent in interest of the first preferred stockholders as represented by the trust receipts hereinabove described. This agreement may also be terminated by the sale of the assets of the Company or by the sale of all the common and preferred stock of the Company, or by the sale of all the common stock of the Company, and by the distribution of the proceeds thereof, as hereinafter provided. In the event of the termination of this agreement other than by such sale of the assets or of the stock of the Company, the Trustees, upon surrender of any trust receipt then outstanding, shall, in accordance with the terms thereof, and out of the stock certificates held by them, deliver stock certificates to the holders of trust receipts in the amounts provided in such trust receipts. Upon or after any such termination of this agreement the Trustees shall instruct the Depositary and Transfer Agent to deliver the said stock certificates in exchange for trust receipts when and as surrendered to said Depos-

itary and Transfer Agent for exchange, as herein provided, and all further liability of the Trustees for the delivery of stock certificates in exchange for trust receipts shall then cease and determine.

3. If the Trustees shall receive dividends in liquidation or otherwise on the shares of stock held by them under this agreement, the holder of trust receipts shall be entitled to receive pro rata distribution therefrom.

4. Any trustee may at any time resign by delivering to the other trustees, or their authorized agent, his resignation in writing to take effect ten days thereafter. In case of the death or resignation or inability to act of any trustee, the vacancy thereby occurring shall be filled by the appointment of a successor or successors to be named by the remaining trustees, provided, however, that Halsey, Stuart & Co., Second Ward Securities Company, Peirce, Fair & Company, and Wells-Dickey Company shall have the right to nominate the successor or successors to the trustee originally appointed by each of said companies respectively.

The Trustees may adopt their own rules of procedure. The action of the majority of the Trustees expressed from time to time at a meeting or by writing or telegram with or without a meeting constitutes the action of the Trustees and has the same effect as though assented to by all. Any trustee may vote or may act in person or by proxy and may be a director or an officer of the Company and vote for himself as such. The Trustees may exercise any power or per-

form any act hereunder by an agent or attorney appointed by them respectively in writing.

5. The Trustees shall have full power at any time to cause the deposited stock certificates to be transferred. As holders of said stock they assume no liability as stockholders, their interest hereunder being that of Trustees only. In voting the deposited stock, the Trustees will exercise their best judgment to secure the election of suitable directors of the Company, to the end that its business and affairs shall be properly managed and in voting and in acting on other matters upon which said Trustees have the power to vote and act hereunder, the Trustees will likewise exercise their best judgment, but they assume no responsibility in respect to such election or management or in respect to any action taken by them or taken in pursuance of their consent thereto and no trustee shall incur any responsibility as stockholder, trustee or otherwise by reason of any error of law or any matter or thing done or suffered or omitted to be done under this agreement, except for his own individual willful malfeasance.

6. All notices to be given to the holders of trust receipts shall be given by registered mail to the holders of trust receipts at the addresses furnished by such holders to the Transfer Agent. Notice to holders of trust receipts whose addresses are not known to the Transfer Agent shall be given by publication in a daily paper of general circulation in the City of Chicago twice in each week for two successive weeks and any call or notice so given shall be taken and considered as though personally served on all the holders of said trust receipts and notices so served shall be the only notice required to be given under any provision of this agreement.

7. In addition to the voting powers and other powers herein conferred upon the said Trustees, the Trustees shall have the discretionary power to sell all of the common and/or preferred stock as a unit but only upon terms which will retire or purchase all of the first preferred stock at not less than par and all accumulated dividends, unless and except otherwise authorized or instructed in writing by not less than 75 per cent in interest of the first preferred stockholders. Provided, however, that in the event of the sale of all or part of the Company's property, or of the first preferred and/or common stock of the Company, at a price sufficient to yield net proceeds in excess of the call price and accumulated dividends of said first preferred stock and said excess is greater than 75 per cent of the par value of the second preferred stock, plus interest on par at 6 per cent from January 1, 1927, then such excess shall be devoted to the purchase or retirement (whichever the Trustees may designate) of said second preferred stock at 75 per cent of par and such interest and if the said excess is not equal to 75 per cent of par and such interest as aforesaid, then each of the holders of the second preferred stock shall have the option (within twenty days of notification thereof) of receiving from such excess the proportion which the second preferred stock par value belonging to him bears to the total amount of second preferred stock par value outstanding in cancellation of or in return for his stock, as said Trustees may determine.

8. The Trustees shall have the power to employ such agents, attorneys and employees as they may deem in their discretion advisable and may fix the compensation of persons so employed and may incur such other ex-

penses as they may in their discretion determine to be necessary or advisable, and may require the Company to pay such compensation and other expenses, including liabilities heretofore incurred by the Bondholders' Protective Committee, together with reasonable compensation to the Trustees, if they so determine, for the services herein required of them and also for the services heretofore performed by the Bondholders' Protective Committee.

9. The term "Company" for the purposes of this agreement, shall be taken to mean the Coos Bay Lumber Company (formerly the Pacific States Lumber Company) a corporation organized under the laws of the State of Delaware, or any successor corporation or corporations, with or into which the same may be consolidated or merged.

IN WITNESS WHEREOF, the parties hereto have hereunto set their hands and seals as of the day and year first above written.

G. S. ARNOLD,
C. T. MacNEILLE,
NEWTON V. WAGNER,
A. McC. WASHBURN,
HOMER W. BUNKER,

Committee.

G. S. ARNOLD,
C. T. MacNEILLE,
NEWTON V. WAGNER,
A. McC. WASHBURN,
HOMER W. BUNKER,

Trustees. [11]

EXHIBIT "C"

TREASURY DEPARTMENT

Washington

MT-M-RHP

C1-M-11969

Mar 3-1930

Coos Bay Lumber Co.,
Balfour Bldg.,
San Francisco, California.

Gentlemen:

Your claim for the redemption of stamps in the amount of \$1,775.13, affixed in payment of tax on issues of stock, has been examined.

The issues in question consisted of 63,757 shares of first preferred stock of a par value of \$100.00 per share, and the same number of shares of common stock of no par value, and 10,000 shares of second preferred stock of a par value of \$100.00 per share. Stamps were affixed with respect to the common stock of no par value based on the actual value of \$30.00 per share.

You ask redemption of the stamps affixed in payment of the tax on the issue of 10,000 shares of second preferred stock on the ground that these shares were issued in exchange for outstanding certificates and the issue did not involve an increase in the capital of the corporation.

You also ask redemption of stamps in the amount of \$1,275.13 affixed with respect to the 63,757 shares of common stock of no par value on the ground that these shares had no actual value at the time of issue, this being evidenced by the fact that they were afterwards sold along with the first preferred stock for a price which covered only the par value of the preferred stock.

The evidence submitted shows that you are correct in your statement that the issue of the second preferred stock in exchange for outstanding shares did not involve an increase in the capital of the corporation, and that the common stock had no actual value at the time of issue. It is disclosed, however, that the 10,000 shares of second preferred stock were not issued to the stockholders but to certain trustees, and that the 63,757 shares of first preferred and 63,757 shares of common stock, which were issued through an agreement with bondholders, were not issued to such bondholders, but to trustees.

The rights of the stockholders and the bondholders to receive these shares of stock were, therefore, transferred, and such transfer is subject to tax under Schedule A-3 of the Revenue Act of 1926. The tax on the transfer of such rights amounts to \$2,750.28. Deducting from this the overpayment of \$1,775.13 on the issue tax, a stamp tax of \$975.15 is still due.

Your claim is therefore rejected, and it is requested that additional stamps in the amount of \$975.15 be affixed.

Respectfully,

ROBT. H. LUCAS

HJB

Commissioner.

[Endorsed]: Filed Jun. 28, 1932. [12]

[Title of Court and Cause.]

ANSWER.

Now comes the defendant and answers the complaint on file herein as follows:

I.

Defendant admits the allegations of paragraphs I and II of the complaint.

II.

Because of his lack of information and belief upon the allegations of paragraph III, defendant denies each and every allegation therein.

III.

Because of his lack of information and belief upon the allegations of paragraph IV, defendant denies each and every allegation therein.

IV.

Because of his lack of information and belief upon the allegations of paragraph V, defendant denies each and every allegation therein.

V.

Because of his lack of information and belief upon the allegations of paragraph VI, defendant denies each and [13] every allegation therein.

VI.

Because of his lack of information and belief upon the allegations of paragraph VII, defendant denies each and every allegation therein.

VII.

Because of his lack of information and belief upon the allegations of paragraph VIII, defendant denies each and every allegation therein.

VIII.

Defendant denies the allegations of paragraph IX.

IX.

Defendant admits the allegations of paragraphs X, XI, XII and XIII.

X.

Answering paragraph XIV, defendant admits that the Commissioner of Internal Revenue in a letter dated March 3, 1930, advised plaintiff that he had determined that stamp taxes in the amount of \$2750.28 should have been paid upon the transfer to said voting trustees by the former bondholders or bondholders' protective committee of said 63,757 shares of preferred stock and said 63,757 shares of common stock. Denies that this determination or claim of the Commissioner was unfounded or erroneous. Defendant denies the allegation that there could be no transfer of said stock. Admits that the Commissioner in said letter determined that stamps in the sum of \$200 should have been affixed to the transfer to Warner as said trustee of said 10,000 shares of second preferred trust, which determination plaintiff did not contest.

Saving as herein expressly admitted, defendant denies the allegations of paragraph XIV. [14]

XI.

Answering paragraph XV, defendant admits that on or about July 15, 1930, plaintiff was notified of an assessment of \$975.15 which was the difference between the tax determination on said transfer of rights (amounting to \$2750.28) and the overpayment of \$1775.13 paid on the issue of stock.

Defendant admits that on July 25, 1930, plaintiff filed with the defendant a claim of abatement of said assessment which was rejected on January 27, 1931. Admits that on February 13, 1931, plaintiff paid to defendant the assessment of \$975.15 and interest thereon in the sum of \$64.76.

Saving as herein expressly admitted, defendant denies each and every allegation of paragraph XV.

XII.

Defendant admits paragraph XVI.

XIII.

Defendant admits that said sum of \$1575.13 and \$1039.91 (aggregating \$2615.04) have not been repaid to plaintiff. Saving for this admission, defendant denies the allegations of paragraph XVII.

XIV.

Admits the allegations of paragraph XVIII.

WHEREFORE defendant prays that the complaint be dismissed and for his costs and for such other relief as may be just.

GEO. J. HATFIELD

United States Attorney

ESTHER B. PHILLIPS

Asst. United States Attorney [15]

United States of America,
Northern District of California,
City and County of San Francisco.—ss.

JOHN P. McLAUGHLIN, being first duly sworn, deposes and says: That he is Collector of Internal Revenue for the First District of California, and defendant in the above entitled action; that he has read the

foregoing answer to the complaint herein and knows the contents thereof; that the same is true of his own knowledge except as to the matters therein stated on information or belief, and that as to those matters he believes it to be true.

JOHN P. McLAUGHLIN

Subscribed and sworn to before me this 3rd day of November, 1932.

[Seal]

JAMES J. SULLIVAN

Notary Public in and for the City and County of San Francisco, State of California.

[Endorsed]: Service of the within Answer by copy admitted this 7th day of November, 1932.

WILLIAM DENMAN

Attorney for Plaintiff.

[Endorsed]: Filed Nov. 7, 1932. [16]

[Title of Court and Cause.]

WAIVER OF JURY.

IT IS HEREBY STIPULATED AND AGREED that the above entitled cause may be tried by the Court sitting without a jury.

Dated, May 10th, 1934.

WILLIAM DENMAN

Attorney for Plaintiff.

H. H. McPIKE,

U. S. Atty.

By ESTHER B. PHILLIPS,

Asst. U. S. Atty.

Attorneys for Defendant.

[Endorsed]: Filed May 10, 1934. [17]

[Title of Court and Cause.]

STIPULATION OF FACTS AND AMENDMENT
OF COMPLAINT.

IT IS HEREBY STIPULATED by and between the parties hereto that, in addition to the facts admitted by the pleadings herein, the following facts are true:

1. That the allegations of Paragraphs III, IV, together with Exhibit "A", which Exhibit "A" is incorporated by reference and made a part of this Stipulation, and also Paragraphs VI and VII of the plaintiff's complaint herein are true.

2. That it is true that said Bondholders' Protective Committee, as stated in Exhibit "A" of the complaint herein, was originally composed of G. S. Arnold, of San Francisco, California; C. T. MacNeille, of Halsey, Stuart & Co., Chicago, Illinois; N. V. Wagner, of Second Ward Securities Co., Milwaukee, Wisconsin; Alexander V. Ostrom, of Wells-Dickey Co., Minneapolis, Minnesota, and Homer W. Bunker, of Peirce, Fair & Co., San Francisco, California, and that prior to the proposed Plan of Reorganization described in Paragraph V of the complaint herein, Alexander V. Ostrom, representing Wells-Dickey Co., of Minneapolis, Minnesota, retired from said Prospective Committee and A. McC. Washburn, representing Wells-Dickey Co., of Minneapolis, Minnesota, became a member of said Committee in his place, this being the only change in the personnel of said Committee. That it is true that said Bondholders' Protective Committee selected itself and no others as managers, and at all times acted as managers, of the Plan of Reorganization described in said

complaint, under which said 63,757 shares of First Preferred Stock and 63,757 shares of No Par Value Common Stock of the Coos Bay Lumber Company, plaintiff herein, were issued. [18]

3. That it is true that pursuant to said Plan of Reorganization the following investment banking firms or houses, Halsey, Stuart & Co., Second Ward Securities Co., Wells-Dickey Co. and Peirce, Fair & Co., acting respectively through their representatives, C. T. MacNeille, N. V. Wagner, A. McC. Washburn and Homer W. Bunker, said representatives being also members of the Bondholders' Protective Committee, did name said representatives, together with said G. S. Arnold, as the Trustees to whom all of said First Preferred and No Par Value Common Stock was to be, and was issued. That since said Trustees to whom the stock was issued were so named by said persons representing said investment banking houses and not by the Bondholders' Protective Committee as such, the allegations of Paragraphs V and VIII of the complaint that the said Trustees were named by the Bondholders' Protective Committee are in error, and it is hereby stipulated and agreed that said Paragraphs V and VIII may be and hereby are deemed amended to allege that the designation of said Trustees was as hereinbefore in this Paragraph 3 set forth, and except as so amended the allegations of Paragraphs V and VIII are true.

4. Attached hereto, marked Exhibit "D" and hereby made a part hereof is the plan of reorganization described and quoted from in paragraph V of the complaint.

5. That it is true that said Trustees, to-wit, G. S. Arnold, C. T. MacNeille, N. V. Wagner, A. McC. Wash-

burn and Homer W. Bunker, held all of said First Preferred and No Par Value Common Stock under the terms of a trust agreement between said Trustees and said Bondholders' Protective Committee, which trust agreement is attached to and made a part of the complaint herein, marked Exhibit "B", and is hereby incorporated by reference and made a part of this [19] Stipulation.

Dated at San Francisco, May 9, 1934.

WILLIAM DENMAN,

Attorney for Plaintiff.

H. H. McPIKE,

U. S. Attorney.

By ESTHER B. PHILLIPS,

Asst. U. S. Attorney.

Attorneys for Defendant. [20]

EXHIBIT "D".

G. S. Arnold, Chairman,	Central Trust Company
C. T. MacNeille,	of Illinois,
N. V. Wagner,	Chicago, Illinois.
A. McC. Washburn,	Second Ward Savings Bank,
Homer W. Bunker,	Milwaukee, Wisconsin.
Committee.	Minneapolis Trust Co.,
Winston, Strawn & Shaw,	Minneapolis, Minn.
38 S. Dearborn Street,	Bank of California, N. A.,
Chicago, Illinois,	San Francisco, California.
Counsel.	Depositories.

PACIFIC STATES LUMBER COMPANY
BONDHOLDERS' PROTECTIVE COMMITTEE
Under Deposit Agreement Dated September 18, 1925
for
FIRST MORTGAGE 8% SERIAL GOLD BONDS
HARRY SMYTH, Secretary,
201 South La Salle Street,
Chicago, Illinois.
ARTHUR N. SELBY, Ass't Sec.,
432 California Street,
San Francisco, Cal.

May 4, 1927.

TO THE DEPOSITING HOLDERS OF
PACIFIC STATES LUMBER COMPANY
FIRST MORTGAGE 8% GOLD BONDS:

Your Committee has diligently endeavored to find a purchaser for the Pacific States Lumber Company on terms assuring the payment of the bonded indebtedness and other liabilities of the Company, plus some consideration acceptable to the stockholders, in order that receivership proceedings and the expense and delay incident thereto might be avoided.

However, we have not been successful in developing a purchaser whose offer we felt justified in accepting, and have terminated all negotiations for any sale.

It is the Unanimous opinion of the Committee that, having failed in the collection of principal and interest of their bonds, the bondholders are entitled to complete possession of their security.

This Committee has therefore devised a plan of reorganization which is appended hereto. The purpose of this plan is to place not only the entire control of

the Company, but also actual ownership thereof in the hands of the bondholders who assent to the plan. It has the unqualified recommendation not only of your Committee, but also of the four banking houses which distributed the bonds, namely, Halsey, Stuart & Co., Second Ward Securities Co., Wells-Dickey Co., and Peirce, Fair & Co.

It is obvious that the support of all bondholders is necessary if this Committee is to put the plan into effect without resorting to receivership and foreclosure of the [21] mortgage, and the otherwise unnecessary expenses incident thereto.

The balance sheet of the Company at March 31, 1927 as submitted to the Committee by the treasurer of the Company is attached hereto.

This plan is submitted to you for your consideration and your attention is called to the provisions of the Deposit Agreement dated September 18, 1925, governing the withdrawal of your bonds if you do not consent. SHOULD YOU APPROVE THIS PROPOSED PLAN NO ACTION ON YOUR PART IS NECESSARY. IN CASE YOU DO NOT APPROVE, THE COMMITTEE MUST BE NOTIFIED IN WRITING WITHIN TWENTY DAYS FROM THE DATE HEREOF AND YOU MAY THEN WITHDRAW YOUR BONDS UPON THE TERMS STATED IN THE DEPOSIT AGREEMENT.

BONDHOLDERS' PROTECTIVE COMMITTEE,

G. S. Arnold, Chairman,

C. T. MacNeille,

N. V. Wagner,

A. McC. Washburn,

Homer W. Bunker. [22]

PACIFIC STATES LUMBER COMPANY
PLAN AND AGREEMENT OF REORGANIZATION
ADOPTED BY THE BONDHOLDERS' PRO-
TECTIVE COMMITTEE APRIL 19, 1927.

1. Recapitalization. All the present stock of Pacific States Lumber Company shall be cancelled, and the Company recapitalized upon the following basis:

\$6,827,700 First Preferred Stock, entitled to dividends at 7%, cumulative from July 1, 1925, redeemable at 105 and accumulated dividends.

\$1,000,000 Second Preferred Stock, entitled to dividends at 6% from and after January 1, 1932, redeemable at par and accumulated dividends, if any.

68,277 shares of No Par Value Common Stock.

Common Stock only shall have voting power, but no dividends shall be paid on Common Stock until January 1, 1933 nor thereafter until all accumulated dividends on Preferred Stocks have been paid, and suitable sinking fund provision made for the retirement of Preferred Stocks in the order of their preference as the property is depleted by the liquidation of assets.

2. Stock Distribution. For each \$100 principal of the present \$6,827,700 of bonds outstanding, there shall be issued in exchange \$100 par value of First Preferred Stock and one share of Common Stock. Any of the authorized First Preferred and Common Stock not so exchanged shall be cancelled.

All of the Second Preferred Stock shall be issued to a Trustee for the former stockholders of all classes to be divided in such proportions as they shall determine.

3. Voting Trust. The First Preferred and Common Stock shall be held and voted by a committee of five Voting Trustees, for the benefit of the owners thereof,

with discretionary power to sell all of the Common and/or First Preferred Stock as a unit, but upon terms which will retire or purchase all of the First Preferred Stock at not less than par and accumulated dividends, unless and except otherwise authorized or instructed in writing by not less than 75% in interest of the First Preferred Stockholders. Also all the assets of the Company may be sold or mortgaged upon majority vote of the Common Stock.

PROVIDED, HOWEVER, that in the event of a sale of all or part of the Company's property, or of the First Preferred and/or Common Stock of the Company (while the First Preferred and Common stock is in the hands of the Trustees, as herein provided) at a price sufficient to yield net proceeds in excess of the call price and accumulated dividends on said First Preferred Stock, and such excess is greater than 75% of the par value of the Second Preferred Stock plus interest at 6% on par from January 1, 1927, then such excess shall be devoted to the purchase or retirement (whichever the trustees may designate) of said Second Preferred Stock at 75% of par and interest; and if said excess is not equal to 75% of par and interest as aforesaid, then each of the holders of the Second Preferred Stock shall have the option (within [23] twenty days of notification thereof) of receiving from such excess the proportion which the Second Preferred Stock par value belonging to him bears to the total amount of Second Preferred Stock par value outstanding in cancellation of or in return for his stock as said trustees may determine.

Each of the investment bankers (Halsey, Stuart & Co., Second Ward Securities Co., Wells-Dickey Co. and Peirce, Fair & Co.,) shall appoint one Voting Trustee

and his respective successors, and the four thus appointed shall select a fifth member as chairman.

The Trustees shall act by majority vote.

Suitable trust certificates, which shall be transferable, shall be prepared by the Trustees and delivered to the persons or parties entitled thereto, in evidence of their beneficial interest in said stock, which shall be deposited with Central Trust Company of Illinois, Chicago, Illinois, as depositary.

Unless dissolved by a sale of the assets of the Company or a sale of the Common Stock or the Common and First Preferred Stock, the Trust shall terminate and the stock shall be distributed to the owners thereof upon the written demand of no less than 75% in interest of the First Preferred stockholders, as represented by voting trust certificates, and, in any event, not later than January 1, 1932.

4. Treasury Bonds. The above investment bankers have agreed as a part of this plan to the surrender for cancellation of the \$573,040 of coupons, secured under the mortgage, and the \$583,000 of Treasury Bonds, likewise secured under the mortgage, held by or for them, leaving them with unsecured 6% serial notes, due January 1, 1928, to January 1, 1932, in connection with their advances to the Company for the protection of the bondholders; the Company to agree to cancel said securities, together with the \$54,000 remaining Treasury Bonds.

5. Time of Taking Effect. No bonds shall be actually exchanged for stock or cancelled, as hereinabove provided, unless and until all outstanding bonds are in the absolute control of the Managers.

6. Foreclosure. In the event that completion of this

plan is obstructed by the refusal of a minority of the bondholders to assent thereto, the Managers in their discretion are empowered to organize a new corporation similarly capitalized, for the purpose of putting the plan into effect and acquiring the assets of the old company on behalf of the assenting bondholders through process of foreclosure proceedings or otherwise.

7. Managers. G. S. Arnold, C. T. MacNeille, Newton V. Wagner, A. McC. Washburn and Homer W. Bunker, constituting the Bondholders' Protective Committee, are hereby appointed managers of this plan of reorganization, with full power and authority to do and perform all acts in relation thereto necessary to complete the same, including the right to amend the same in minor particulars without notice.

8. Termination. The authority of the Managers shall be coextensive as to time with that of the Bondholders' Protective Committee. [24]

PACIFIC STATES LUMBER COMPANY

And Subsidiary Companies

Condensed Consolidated Balance Sheet, March 31, 1927

ASSETS

Current Assets—

Cash	\$ 105,634.12	
Receivables (Less Reserves).....	661,075.05	
Inventories (Lower of Cost or Market).....	1,860,793.85	
		<hr/>
Total Current Assets.....		\$ 2,627,503.02
Miscellaneous Funds		3,317.85
Investments		11,505.00
Sinking Fund on deposit with Central Trust Company of Illinois, Trustee for First Mort- gage 8% Bonds.....		766,165.36
Timber and Lands (at Book Values).....		10,481,212.96
Plants, Equipment, Railroads, Steamers, etc.—		
Cost	\$9,706,914.56	
Less: Reserve for Depreciation.....	3,977,891.50	5,729,023.06
		<hr/>
Deferred Charges to Future Operations.....		87,381.66
		<hr/>
Total Assets		\$19,706,108.91
		<hr/>

LIABILITIES

Current Liabilities—

Secured Bank Loans.....	\$ 381,720.00	
Due for Amounts Advanced by Bankers for Protection of Bondholders—		
Coupons Purchased	\$573,040.00	
Secured Loans	375,000.00	948,040.00
Contracts and Other Notes Payable.....		136,293.75
Trade Accounts Payable, Wages and Sundry Accrued Items.....		356,258.04
Accrued Property Taxes.....		187,887.01
Total Current Liabilities.....		\$ 2,010,198.80

Contingent Liabilities—

Pending Litigation\$ 25,000.00

Deferred Liabilities, etc..... 8,596.83

First Mortgage 8% Gold Bonds.....

	Par	Premium	Total	
Due January 1, 1927....	\$ 164,700.00	\$ 4,117.50	\$ 168,817.50	
Due January 1, 1932....	1,000,000.00	50,000.00	1,050,000.00	
Due January 1, 1937....	1,500,000.00	112,500.00	1,612,500.00	
Due January 1, 1942....	4,800,000.00	480,000.00	5,280,000.00	
	\$7,464,700.00	\$646,617.50	\$8,111,317.50	
Less in Treasury.....	637,000.00	63,700.00	700,700.00	
	\$6,827,700.00	\$582,917.50	\$7,410,617.50	
Interest Accrued from July 1, 1925.....		955,878.00	8,366,495.50	
Total Liabilities			\$10,385,291.13	

Net Worth

Capital Stock Outstanding—

7% Cumulative Preferred "A".....	\$166,700.00	
8% Cumulative Preferred "B".....	150,000.00	
8% Cumulative Preferred "C".....	113,333.33	
Common	998,400.00	\$1,428,433.33

Surplus, including Capital Surplus.....	7,892,384.45	9,320,817.78
Total Liabilities and Net Worth....		\$19,706,108.91

The above Condensed Consolidated Balance Sheet of the Pacific States Lumber Company has been compiled from the books of the Company and in my opinion correctly sets forth the consolidated financial position of the Company as at March 31, 1927.

A. H. PAULSEN,
Treasurer.

(Endorsed): Filed May 10, 1934.

District Court of the United States, Northern District
of California, Southern Division.

AT A STATED TERM of the Southern Division of the United States District Court for the Northern District of California held at the Court Room thereof, in the City and County of San Francisco, on Thursday, the 22nd day of November, in the year of our Lord one thousand nine hundred and thirty-four.

PRESENT: the Honorable Frank H. Kerrigan, District Judge.

[Title of Cause.]

This case having been heretofore submitted and due consideration having been had it is ordered that Judgment be entered in favor of Plaintiff for the sum of \$2615.04, with interest at 6% per annum, thereon, as follows: on \$1575.13, from Feb. 25, 1928; on \$1039.91 from Feb. 11, 1931; together with costs of suit. Further the case having been submitted on stipulated facts, no findings of fact or conclusions of law are necessary.

[26]

In the Southern Division of the United States District
Court for the Northern District of California.

No. 19268-K

COOS BAY LUMBER COMPANY, a corporation,
Plaintiff,

vs.

JOHN P. McLAUGHLIN, as United States Collector
of Internal Revenue, First District of California,
Defendant.

JUDGMENT.

This cause having come on regularly for trial on the 10th day of May, 1934, before the Court sitting without a Jury, a trial by Jury having been waived by written stipulation filed; Lyman T. Henry, Esquire, appearing as attorney for plaintiff, and Esther B. Phillips, Assistant United States Attorney, appearing as attorney for defendant, and the trial having been proceeded with and a Stipulation of Facts having been filed, and the cause having been submitted to the Court for consideration and decision, and the Court, after due deliberation having rendered its decision and ordered that judgment be entered herein in favor of plaintiff for the sum of \$2615.04, with interest at the rate of 6% per annum, as follows: on \$1575.13, from Feb. 25, 1928, until paid, on \$1039.91, from Feb. 11, 1931, until paid,

and for costs:

Now, therefore, by virtue of the law and by reason of the premises aforesaid, it is considered by the Court that Coos Bay Lumber Company, a corporation, plaintiff, do have and recover of and from John P. McLaughlin, as United States Collector of Internal Revenue,

First District of California, Defendant, the sum of \$2615.04, with interest at the rate of 6% per annum, as follows: on \$1575.13, from Feb. 25, 1928, until paid, on \$1039.91, from Feb. 11, 1931, until paid, together with its costs herein expended taxed at \$10.00.

Judgment entered this 22nd day of November, 1934.

WALTER B. MALING,

Clerk. [27]

[Title of Court and Cause.]

BILL OF EXCEPTIONS.

BE IT REMEMBERED that on the 10th day of May, 1934, the above-entitled case came regularly on for trial before the Court, sitting without a jury, trial by jury having been expressly waived. The plaintiff appeared by its Attorneys, WILLIAM DENMAN and LYMAN HENRY, and the defendant appeared by his Attorneys, H. H. McPIKE, United States Attorney, and ESTHER B. PHILLIPS, Assistant United States Attorney, and the following proceedings were had:

The plaintiff offered in evidence a Stipulation of Facts, signed and agreed to by both parties, which was regularly on file in the records of the case. Said Stipulation of Facts is hereby incorporated into this Bill of Exceptions by reference and made a part of it. Thereupon the plaintiff rested. The defendant rested. Plaintiff moved for judgment in its favor and moved the Court to conclude from the stipulated facts that as a matter of law the newly created trustees referred to in said Stipulation of Facts were the only persons who ever had a right to receive the stock in question; that there never was a transfer to them by the bondholders or any other person or body of a right to receive said

stock, and that the transaction did not constitute a taxable transaction. The [28] defendant moved for judgment in his favor, and further moved the Court to conclude from the stipulated facts that as a matter of law the bondholders referred to in said Stipulation of Facts had a right to receive the stock issued in consideration for their bonds and transferred to the newly created trustees such right, and that said transaction constituted a taxable transaction. The Court took the motions of Plaintiff and Defendant under submission. Thereafter briefs were submitted.

The Court, having considered the evidence and the arguments of counsel, on the 22nd day of November, 1934, granted the Plaintiff's motions, to which the defendant duly excepted, and defendant hereby assigns said exception as Defendant's Exception No. 1. The Court, on said 22nd day of November, 1934, denied defendant's motions. The defendant excepted and hereby assigns said exception as Defendant's Exception No. 2. The Court thereupon ordered judgment to be entered in favor of plaintiff. Said order appears elsewhere in the record and by reference is made a part of this Bill of Exceptions.

WHEREFORE defendant, within the time required by law and the rules of court, presents this Bill of Exceptions, and prays that the same be settled, allowed and approved by the Court.

H. H. McPIKE,

United States Attorney.

By ESTHER B. PHILLIPS,
Asst. United States Attorney,
Attorneys for Defendant. [29]

[Title of Court and Cause.]

STIPULATION RE BILL OF EXCEPTIONS.

It is hereby STIPULATED and AGREED by and between the attorneys for plaintiff and for the defendant that the foregoing Bill of Exceptions has been presented within the term of Court, as required by law and the rules of this Court, and that it is proper for said Bill of Exceptions to be approved, allowed and settled as correct in all respects.

WILLIAM DENMAN,
LYMAN HENRY,

Attorney for Plaintiff.

H. H. McPIKE,

United States Attorney.

ESTHER B. PHILLIPS,
Asst. United States Attorney.
Attorneys for Defendant.

ORDER SETTLING BILL OF EXCEPTIONS.

The foregoing Bill of Exceptions contains all of the evidence offered upon said cause. It is hereby approved and settled as correct in all respects.

A. F. ST. SURE,
United States District Judge. [30]

[Title of Court and Cause.]

ORDER SETTLING BILL OF EXCEPTIONS.

The above-entitled cause came on for hearing on the application of the defendant to settle the Bill of Exceptions in this case, and it appearing to the Court that said Bill of Exceptions contains all of the material facts

occurring upon the trial of the cause, and all the evidence adduced at the same, and that the parties hereto have stipulated and agreed upon said Bill;

And it FURTHER APPEARING that said cause was heard and judgment therein rendered by the Honorable Frank H. Kerrigan, United States District Judge for the Northern District of California, and that by reason of the death of the said Honorable Frank H. Kerrigan, on or about the 9th day of February, 1935, said Bill of Exceptions cannot be allowed by the Judge before whom said cause was tried;

And it FURTHER APPEARING from the records of said cause, and from the stipulation of counsel for both parties, a true bill of exceptions can be allowed and fairly passed upon.

NOW, THEREFORE, it is hereby ORDERED that the foregoing Bill of Exceptions be and the same is hereby settled as a true Bill of Exceptions in said cause, and that it contains all of the material facts, matters, things and exceptions occurring upon the trial of said cause, and the same is hereby certified accordingly by the undersigned Judge of this Court in the place and stead of the Honorable Frank H. Kerrigan.

Dated: February 15, 1935.

A. F. ST. SURE,
United States District Court.

[Endorsed]: Filed Feb. 15, 1935. [31]

[Title of Court and Cause.]

PETITION FOR APPEAL AND ORDER
ALLOWING APPEAL.

To the Honorable Judges of the United States District
Court for the Northern District of California:

The defendant herein, feeling aggrieved by the judgment entered in this cause, on or about November 22, 1934, against him, does hereby appeal from such judgment to the United States Circuit Court of Appeals for the Ninth Circuit for the reasons set forth in the Assignment of Errors filed herewith, and prays that this appeal be allowed; that citation be issued, as provided by law; that a transcript of the record, proceedings and documents, upon which said judgment was based, duly authenticated, be sent to said Circuit Court of Appeals for the Ninth Circuit, under the rules of said court, and that no bond or other security be required of defendant Collector of Internal Revenue upon said appeal.

H. H. McPIKE,

United States Attorney.

By ESTHER B. PHILLIPS,

Assistant United States Attorney.

Attorneys for Defendant.

ORDERED that the appeal be allowed and that [32] defendant shall not be required to give any bond or other security upon said appeal.

Dated: February 20, 1935.

A. F. ST. SURE,

United States District Judge.

[Endorsed]: Service of the within Petition by copy admitted this 20th day of Feb. 1935.

LYMAN HENRY,
Attorney for Plf.

[Endorsed]: Filed Feb. 20, 1935. [33]

[Title of Court and Cause.]

ASSIGNMENT OF ERRORS.

To the Honorable Judges of the United States Circuit Court of Appeals for the Ninth Circuit:

Comes now the defendant, JOHN P. McLAUGHLIN, as Collector of Internal Revenue for the First Collection District of California, and files the following assignment of errors, upon which he will rely in his petition for review of the judgment heretofore entered in this cause by the United States District Court for the Northern District of California:

I.

The Court erred in entering its decision and judgment in favor of plaintiff and against defendant in the sum of \$2,615.04, with interest thereon.

II.

The Court erred in granting plaintiff's motion for judgment in its favor.

III.

The Court erred in its conclusions from stipulated facts that as a matter of law, the newly created trustees referred to in the Stipulation of Facts were the only

persons who ever had a right to receive the stock in question; that there never was a transfer to them by the bondholders, or any other person or body of a right to receive said stock and that [34] the transaction did not constitute a taxable transaction.

IV.

The Court erred in denying the defendant's motion for judgment in his favor.

V.

The Court erred in refusing to conclude from the stipulated facts that as a matter of law the bondholders referred to in said stipulation had a right to receive the stock issued in consideration for their bonds and transferred to the newly created trustees such right and that said transaction constituted a taxable transaction.

H. H. McPIKE,

United States Attorney,

ESTHER B. PHILLIPS,

Assistant United States Attorney.

(Attorneys for Defendant)

[Endorsed]: Service of the within Assignment by copy admitted this 20th day of Feb. 1935.

LYMAN HENRY,

Attorney for Plf.

[Endorsed]: Filed Feb. 20, 1935. [35]

[Title of Court and Cause.]

NOTICE OF APPEAL.

To plaintiff above-named and to Messrs. William Denman and Lyman Henry, Attorneys for Plaintiff:

Please take notice that the defendant herein hereby appeals to the United States Circuit Court of Appeals for the Ninth Circuit from the judgment entered in this case on or about November 22, 1934.

H. H. McPIKE,

United States Attorney.

By ESTHER B. PHILLIPS,

Assistant United States Attorney.

(Attorneys for Defendant)

[Endorsed]: Service of the within Notice by copy admitted this 20th day of Feb. 1935.

LYMAN HENRY,

Attorney for Plf.

[Endorsed]: Filed Feb. 20, 1935. [36]

[Title of Court and Cause.]

PRAECIPE FOR TRANSCRIPT OF RECORD.

To the Clerk of the above-entitled Court:

Please prepare and transmit to the Clerk of the United States Court of Appeals for the Ninth Circuit a transcript of the record in the above-entitled cause for the use of said Court, including therein the following:

- (1) The judgment roll.
- (2) Stipulation of Facts.

(3) Minute Order of Judgment, and Opinion of Court, if any.

(4) Bill of Exceptions.

(5) Assignment of Errors.

(6) Petition and Order Allowing Appeal.

(7) Notice of Appeal.

(8) Citation on Appeal.

(9) This Praecipe.

H. H. McPIKE,

United States Attorney.

By ESTHER B. PHILLIPS,

Assistant United States Attorney.

(Attorneys for Defendant)

[Endorsed]: Service of the within Praecipe by copy admitted this 20th day of Feb. 1935.

LYMAN HENRY,

Attorney for Plf.

[Endorsed]: Filed Feb. 20, 1935. [37]

[Title of Court and Cause.]

CERTIFICATE OF CLERK, U. S. DISTRICT
COURT TO TRANSCRIPT OF RECORD.

I, WALTER B. MALING, Clerk of the District Court of the United States, in and for the Northern District of California, do hereby certify the foregoing 37 pages, numbered from 1 to 37 inclusive, to be a full, true and correct copy of the record and proceedings as enumerated in the praecipe for record on appeal, as the same remain on file and of record in the above-entitled suit, in the office of the Clerk of said Court, and that the

same constitutes the record on appeal to the United States Circuit Court of Appeals for the Ninth Circuit.

I further certify that the cost of the foregoing transcript of record is \$13.95; that said amount has been charged against the United States and the original Citation issued in said suit is hereto annexed.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed the seal of said District Court this 9th day of April, 1935.

[Seal]

WALTER B. MALING, Clerk.

By J. P. Welsh,

Deputy Clerk. [38]

United States of America, ss:

THE PRESIDENT OF THE UNITED STATES
OF AMERICA

To COOS BAY LUMBER COMPANY, a corporation,
GREETING:

YOU ARE HEREBY CITED AND ADMONISHED to be and appear at a United States Circuit Court of Appeals for the Ninth Circuit, to be holden at the City of San Francisco, in the State of California, within thirty days from the date hereof, pursuant to an order allowing an appeal, of record in the Clerk's Office of the United States District Court for the Northern District of California wherein JOHN P. McLAUGHLIN is appellant, and you are appellee, to show cause, if any there be, why the decree or judgment rendered against the said appellant, as in the said order allowing appeal mentioned, should not be corrected, and why speedy justice should not be done to the parties in that behalf.

WITNESS, the Honorable A. F. ST. SURE, United States District Judge for the Northern District of California this 20th day of February, A. D. 1935.

A. F. ST. SURE,
United States District Judge.

Service of the within Citation by copy admitted this 20th day of Feb. 1935.

LYMAN HENRY,
Attorney for Plf.

[Endorsed]: Filed Feb. 20, 1935. Walter B. Maling, Clerk. B. E. O'Hara, Deputy Clerk. [39]

[Endorsed]: No. 7832. United States Circuit Court of Appeals for the Ninth Circuit. John P. McLaughlin, as United States Collector of Internal Revenue, First District of California, Appellant, vs. Coos Bay Lumber Company, a corporation, Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the Northern District of California, Southern Division.

Filed April 10, 1935.

PAUL P. O'BRIEN,
Clerk of the United States Circuit Court of Appeals
for the Ninth Circuit.

No. 7832

IN THE
United States Circuit Court of Appeals
For the Ninth Circuit

JOHN P. McLAUGHLIN, as United States
Collector of Internal Revenue, First
District of California,

Appellant,

VS.

COOS BAY LUMBER COMPANY
(a corporation),

Appellee.

On Appeal from the District Court of the United States for the
Northern District of California, Southern Division.

BRIEF FOR APPELLANT.

H. H. McPIKE,

United States Attorney,

FRANK J. WIDEMAN,

Assistant Attorney General,

SEWALL KEY,

ANDREW D. SHARPE,

E. F. McMAHON,

Special Assistants to the Attorney General,

Post Office Building, San Francisco,

Attorneys for Appellant.

FILED

NOV 4 - 1935

PAUL P. O'BRIEN,

CLERK

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No. 7832

IN THE

United States Circuit Court of Appeals

For the Ninth Circuit

JOHN P. McLAUGHLIN, as United States
Collector of Internal Revenue, First
District of California,

Appellant,

VS.

COOS BAY LUMBER COMPANY
(a corporation),

Appellee.

On Appeal from the District Court of the United States for the
Northern District of California, Southern Division.

BRIEF FOR APPELLANT.

This is an appeal from the judgment entered by the District Court on November 22, 1934, in favor of the appellee, plaintiff below, and against the appellant, defendant below, permitting recovery in an action at law of \$2615.04, documentary Internal Revenue stamp taxes and interest, assessed against and paid to appellant by appellee for the taxable period February, 1928, together with interest and costs. (R. 50-51.) Petition for appeal, assignments of error, notice, and citation on appeal, were filed by appellant

on February 20, 1935. (R. 55-61.) The appeal was allowed by the District Court on that date. (R. 55.)

The jurisdiction of this Court is invoked under Section 128 (a) of the Judicial Code, as amended by the Act of February 13, 1925, c. 229, 43 Stat. 936.

QUESTION PRESENTED.

Whether the transactions involved constitute taxable transfers, by the former bondholders of the Pacific States Lumber Company, whose name was subsequently changed to Coos Bay Lumber Company, to their trustees, or nominees, of legal title to, or their respective rights to subscribe for, or to receive legal title to, and the 63,757 shares of first preferred, \$100 par value, stock and 63,757 shares common, no par value, stock of Coos Bay Lumber Company, issued direct to such trustees, or nominees, in conformity with certain agreements and a plan of reorganization, in consideration for said bondholders' bonds, within the meaning of the provisions of Section 800 and Schedule A-3, Title VIII, of the Revenue Act of 1926, and Regulations 71, Articles 31 to 34, inclusive, particularly Article 34 (t). No opinion was rendered by the District Court.

STATUTES AND REGULATIONS INVOLVED.

The pertinent provisions of the statutes and regulations involved are set forth in the appendix, *infra*.

STATEMENT OF THE CASE.

This action at law was instituted in the United States District Court for the Northern District of California, Southern Division, on June 28, 1932, by Coos Bay Lumber Company, formerly Pacific States Lumber Company, a corporation, appellee herein, plaintiff below, against John P. McLaughlin, Collector of Internal Revenue, appellant herein, defendant below, for the recovery of \$2615.04, assessed documentary stamp taxes and interest in the amounts of \$2550.28 and \$64.76, respectively, imposed at the rate of 2 cents per share, on the claimed transfer by the owners, or holders, of bonds of the Pacific States Lumber Company, to the trustees, or nominees, of said bondholders, of legal title to, or their respective rights to subscribe for, or to receive legal title to, and the 127,500 shares of stock of Coos Bay Lumber Company, upon issuance in consideration for their bonds, under the provisions of Section 800 and Schedule A-3, Title VIII, of the Revenue Act of 1926.

The appellee's complaint (R. 1-34) alleges that it had been illegally required to pay an assessment of documentary stamp taxes and interest in the aggregate of \$2615.04, no stamps having been purchased, affixed, and cancelled, by reason of such claimed transfer by such bondholders to their trustees, or nominees, in consideration for the bonds of said bondholders; that said trustees received and held said stock as an original issue and not by transfer in any wise from any persons whomsoever; and that said tax was erroneously and illegally assessed and collected, was filed

on June 28, 1932. On November 7, 1932, the appellant filed his answer (R. 34-38) to said complaint in the form of a general issue plea. On May 10, 1934, the parties filed their stipulation of facts and amendment of complaint (R. 39-48), written waiver of jury (R. 38), and the case was tried to the court without a jury on that date. (R. 51.) The stipulation of facts and amendment of complaint (R. 39-48) was offered and received in evidence on behalf of the appellee, without objection. Thereupon, both parties rested and the appellee moved for judgment in its favor and moved the court to conclude from the stipulated facts that as a matter of law the newly created trustees referred to in said stipulation of facts were the only persons who ever had a right to receive the stock in question, that there never was a transfer to them by the bondholders or any other person or body of a right to receive said stock, and that the transaction did not constitute a taxable transaction. Thereupon, the appellant moved for judgment in his favor, and further moved the court to conclude from the stipulated facts that as a matter of law the bondholders referred to in said stipulation of facts had a right to receive the stock issued in consideration for their bonds and transferred to the newly created trustees such right, and that said transaction constituted a taxable transaction. Thereupon, the court took the motions of plaintiff and defendant under submission and thereafter briefs were submitted by the parties. (R. 51-52.)

On November 22, 1934, the court granted the appellee's motions, to which the appellant duly excepted,

and the appellant assigned said exception as appellant's exception No. 1. On November 22, 1934, the court denied appellant's motions and the appellant excepted and assigned said exception as appellant's exception No. 2. (R. 51-52.) The court thereupon ordered judgment to be entered in favor of the appellee and against the appellant, without opinion, findings of fact and conclusions of law. (R. 49, 52.) On November 22, 1934, the Clerk of the District Court entered a formal judgment in favor of the appellee and against the appellant in the sum of \$2615.04, with interest at the rate of 6 per cent per annum on \$1575.13 from February 25, 1928, until paid, and \$1039.91 from February 11, 1931, until paid, together with costs taxed \$10. (R. 50-51.) Thereupon the appellant filed his bill of exceptions (R. 51-52), stipulation of the parties in re bill of exceptions, and orders settling bill of exceptions which were allowed and approved by the court on February 15, 1935. (R. 53-54.) On February 20, 1935, the appellant filed his petition for appeal (R. 55), assignment of errors (R. 56-57), notice of appeal (R. 58), praecipe for transcript of record (R. 58-59), clerk's certificate (R. 59-60), and citation (R. 60-61), which were approved and allowed by the court, without bond or other security, on that date. (R. 55.)

The detailed facts are set forth in the complaint (R. 1-12) and Exhibits A (R. 13-23), B (R. 24-32), and C (R. 33-34), thereto attached, the answer (R. 34-38), the stipulation of facts and amendment of complaint and Exhibit D (R. 39-48), thereto attached, and are in substance as follows:

On September 18, 1925, the Pacific States Lumber Company, whose name was subsequently changed to Coos Bay Lumber Company, had issued and outstanding its first mortgage bonds in the principal amount of \$7,000,000 and was in default in payment of principal and interest. (R. 2.) This amount of outstanding bonds was subsequently reduced to \$6,375,700. (R. 5.)

In September, 1925, there was organized a Bondholders' Protective Committee and on September 18, 1925, such committee and the bondholders of Pacific States Lumber Company, entered into an agreement (R. 13-23), providing for the transfer, assignment, delivery, and deposit of all of their said bonds, including title and all rights and powers of every kind and description given by law, or by the terms of said bonds or any instrument securing the same, except the beneficial ownership thereof, to and with said Bondholders' Protective Committee, for the purposes therein specified, in exchange for negotiable receipts to be issued, by the specified depository receiving such bonds, to such bondholder, each of whom, upon accepting such negotiable receipts, and all transferees thereof, become fully bound by and a party to such agreement, the same as if each had signed the same. (R. 2, 3, 13-23.)

On April 19, 1927, said Bondholders' Protective Committee adopted a plan and agreement of reorganization of Pacific States Lumber Company (R. 44-48), which provided for the cancellation of all of the outstanding stock of Pacific States Lumber Company;

the issuance of first preferred stock, 7 per cent cumulative, in the amount of \$6,827,700; second preferred stock, 6 per cent dividend paying, redeemable at par and accumulations, in the amount of \$1,000,000; and 68,277 shares of no par value common stock of such corporation. All of the first preferred stock and common stock were to be issued, share and share alike, in exchange for each \$100 principal of such outstanding bonds, to trustees of such bondholders, and any of such stock not so issued was to be cancelled. All of the second preferred stock was to be issued to a trustee for the former stockholders of such corporation, of all classes, and divided in such proportion as such classes determine. In addition, such plan and agreement provided for the creation of a trust to receive, hold, and vote such first preferred and common stock for the benefit of the owners thereof, with discretionary power to sell all or either as a unit, upon terms sufficient to retire or purchase all of the first preferred stock at not less than par and accumulated dividends, unless otherwise authorized or instructed by 75 per cent of the first preferred stockholders. Such plan also provided for the sale or mortgaging of all the assets of the company upon a majority vote of such common stock and the appointment by the four investment bankers, who were the owners or holders of said outstanding bonds, of four voting trustees and their respective successors, with power in such trustees to select and appoint a fifth trustee as chairman. Such plan and agreement contained the further provisions: that suitable trust certificates,

representing such stock, which are transferable, shall be prepared, issued, and delivered by such trustees to such bondholders, or persons, or parties, entitled thereto, as evidence of their beneficial interest in said stock, and that the members of such Bondholders' Protective Committee shall constitute the managers of such plan of reorganization with full power to perform any and all acts necessary to complete the same. (R. 44-48.)

The plan and agreement adopted on April 19, 1927, by the Bondholders' Protective Committee, was adopted, ratified, approved, consented to, and agreed to, by each of such bondholders, as therein provided and in conformity with the letter transmitting the same, and such bondholders named the members of such Bondholders' Protective Committee as their trustees under such trust agreement. (R. 40.)

On January 27, 1928, the Bondholders' Protective Committee, by resolution, requested the Pacific States Lumber Company to complete its corporate reorganization in accordance with such plan and agreement and to issue 63,757 shares of its first preferred stock and 63,757 shares of its no par value common stock to the trustees named pursuant to Section 3 of said plan and agreement. On that date the directors of plaintiff corporation, by resolution, duly adopted, spread such request upon its records and empowered and instructed its officers to carry out all of the acts provided in such plan and agreement to be performed by such corporation. (R. 5.)

On February 15, 1928, the Pacific States Lumber Company changed its corporate name to Coos Bay Lumber Company, the appellee herein. (R. 2.)

On February 23, 1928, the members of such Bondholders Protective Committee, as such, entered into the Stock Trust Agreement of Coos Bay Lumber Company (R. 24-32), with themselves as managers and trustees under the trust agreement hereinbefore mentioned, wherein, among other matters and things it is provided (R. 24-25) :

Whereas, the Committee has caused to be delivered to said trustees, certificates representing 63,757 shares of the first preferred stock and an equal number of shares of no par value common stock of Coos Bay Lumber Company (formerly Pacific States Lumber Company) to be held by said trustees for and on behalf of the beneficial owners thereof as designated by the Committee.

Now, therefore, it is agreed as follows:

1. The Trustees shall issue trust receipts and cause the same to be delivered to said beneficial owners, the form thereof to be substantially, as follows:

“No.....Units

Coos Bay Lumber Company

First Preferred and Common Stock Trust Receipt

This Certifies that as hereinafter provided and on surrender thereof..... will be entitled (out of certificates hitherto delivered to the undersigned trustees under the agreement hereinafter mentioned) to receive certificates for.....shares of 7% first

preferred stock with dividends cumulative from July 1, 1925 and for an equal number of shares of no par value common stock of Coos Bay Lumber Company (formerly Pacific States Lumber Company) and to receive payments equal to any dividends which may be collected by the Trustees upon such shares of stock received and held by the Trustees under said agreement.

This receipt is issued pursuant and subject to an agreement dated February 23, 1928 and executed by and between * * *, the Pacific States Lumber Company Bondholders' Protective Committee and * * *, Trustees, * * *."

On or about February 25, 1928, the Coos Bay Lumber Company issued 63,757 shares of its first preferred stock and 63,757 shares of its no par value common stock to said Trustees, to whom said stock was to be, and was issued in accordance with said agreements, resolutions, and said plan and agreement of reorganization, in one certificate, and at the same time such corporation issued to F. A. Warner, as trustee for the former stockholders of Pacific States Lumber Company, 10,000 shares of its second preferred stock, in accordance with said agreements, resolutions, and plan and agreement, in one certificate. (R. 6.)

Thereafter the Commissioner of Internal Revenue assessed documentary stamp taxes against the appellee corporation, on such transfer by the bondholders of the Pacific States Lumber Company, or their Bondholders' Protective Committee, to their trustees, of legal title to, or their respective rights to receive legal title to, and the stock issued by Coos Bay Lumber

Company, in consideration for the bonds of Pacific States Lumber Company, in the amount of \$2550.28, and a like tax of \$200 on the transfer by the former stockholders of Pacific States Lumber Company to their trustee, F. A. Warner, of legal title to, or their respective rights to receive legal title to, and the stock issued by Coos Bay Lumber Company direct to such trustee, in consideration for their Pacific States Lumber Company stock, which was paid to the appellant, Collector of Internal Revenue, in the amount of \$2750.28 together with interest in the amount of \$64.76, by application of a credit of \$1575.13 and cash in the amount of \$1239.91, aggregating in all \$2815.04, on February 25, 1928, and February 11, 1931, respectively. (R. 10, 36-37.)

On February 24, 1931, the appellee corporation filed its claim for refund No. 23104 of tax so paid in the amount of \$2615.04, being the amount of \$2815.04, less the \$200 paid on the transfer by the former stockholders of Pacific States Lumber Company to their trustee, of legal title to, or their respective rights to receive legal title to, and the stock issued in consideration for their surrendered and cancelled stock, which the appellee herein admits was due thereon, on the grounds that such trustees had the original right to receive the other stock issued and no transfer of a right to receive occurred, which was duly rejected by the Commissioner of Internal Revenue on May 3, 1932, on the grounds that the evidence discloses the 10,000 shares of second preferred stock were not issued to the stockholders but to certain trustees, and that the

63,757 shares of first preferred stock and 63,757 shares of common stock, which were issued through an agreement with bondholders, were not issued to such bondholders but to trustees and that the rights of the stockholders and the bondholders to receive these shares of stock were, therefore, transferred and such transfer is subject to tax under Schedule A-3, of the Revenue Act of 1926. (R. 10-11, 33-34.)

SPECIFICATION OF ERRORS TO BE URGED.

The errors assigned and upon each of which appellant relies, numbered I to V, inclusive, are found in the record, pages 56-57, and are incorporated herein by reference.

All of the assignments of error are argued under the question presented in this case, and relied upon the same as if herein fully set out.

ARGUMENT.

At the outset, if the stipulated and admitted facts in this case (R. 1-48) are considered to be the equivalent of either an agreed statement of ultimate facts or an agreed statement of evidentiary facts, the review, in any event, extends to a determination of the question of whether the agreed facts support the judgment (*Supervisors v. Kennicott*, 103 U. S. 554; *Kansas City Life Ins. Co. v. Shirk*, 50 F. (2d) 1046 (C. C. A. 10th); *Lumbermen's Trust Co. v. Town of Ryegate*,

61 F. (2d) 14 (C. C. A. 9th); *Kirkman v. Farmers' Sav. Bank*, 28 F. (2d) 857 (C. C. A. 8th)), and may extend to all questions of law. *Kearney v. Case*, 12 Wall. 275; *United States v. Eliason*, 16 Pet. 291; *Campbell v. Boyreau*, 21 How. 223; *Supervisors v. Kennicott*, *supra*. However, the review with the motions for judgment and exceptions saved (R. 52) extends to a determination of whether the general finding, if any made by the court, is supported by the stipulated facts and whether all of the questions of law have been properly decided. *Maryland Casualty Co. v. Jones*, 279 U. S. 792; *St. Louis v. Western Union Telegraph Co.*, 148 U. S. 92; *Bank of Watertown v. Fidelity & Deposit Co.*, 299 Fed. 478 (C. C. A. 5th), certiorari denied, 266 U. S. 618; *Dunsmuir v. Scott*, 217 Fed. 200 (C. C. A. 9th); *McLaughlin v. Pacific Lumber Co.*, 66 F. (2d) 895 (C. C. A. 9th), reversed, 293 U. S. 351; *United States v. Jefferson Electric Co.*, 291 U. S. 386.

In this connection, if the stipulated facts are considered an agreed statement of ultimate facts, no findings of fact were necessary. However, an examination of the admitted and stipulated facts does not disclose that the appellant either admitted or stipulated that "no transfer of legal title to, or any rights to receive legal title to, or the actual shares or certificates of stock issued was in fact made or effected". Hence, the judgment entered is not sustained by any finding of ultimate fact. On the other hand, if the stipulated facts are considered an agreed statement of evidentiary facts, which they unquestionably are, findings

of fact were necessary. (R. S. 649 (U. S. C., Title 28, Sec. 773); *Insurance Co. v. Boon*, 95 U. S. 117.) However, no findings of fact were made by the court (R. 49), hence, it necessarily follows that the judgment (R. 50) is not supported by any findings of fact.

Thus it is seen that the judgment entered by the District Court is not supported by any ultimate finding and should be reversed (*Universal Battery Co. v. United States*, 281 U. S. 580; *Routzahn v. Willard Storage Battery Co.*, 291 U. S. 386, 410) unless the minute order (R. 49) is considered the equivalent of a general ultimate finding regardless of the provisions thereof to the contrary in which event, it cannot be fairly said such adverse finding naturally follows or flows from the admitted and stipulated facts as a natural inference when such facts are all to the contrary, and the evidence (R. 1-48) fails to disclose either any sufficient or any substantial evidence to sustain such adverse finding or conclusion. Hence, the judgment (R. 50) should be reversed in any event. However, should the court determine further consideration of this case necessary, then the following argument applies.

The transactions involved constitute taxable transfers by the Bondholders of the Pacific States Lumber Company to their Trustees, or Nominees, of legal title to, or their respective rights to subscribe for, or to receive legal title to, and the 127,514 shares of First Preferred and No Par Value Common stock issued direct by the Coos Bay Lumber Company to such Trustees, or Nominees, in conformity with certain agreements and

plan of reorganization in consideration for said Bondholders' bonds, within the meaning of the provisions of Section 800 and Schedule A-3, Title VIII, of the Revenue Act of 1926, and Articles 31-34, of Treasury Regulations 71 promulgated thereunder.

The appellee, plaintiff below, contends that the newly created trustees referred to in the stipulation of facts were the only persons who ever had a right to receive the stock issued direct to them by the Coos Bay Lumber Company in consideration for the bonds issued by the Pacific States Lumber Company; that there never was a transfer to them by the bondholders, or any other person, or body of a right to receive said stock; and that the transaction did not constitute a taxable transfer. The appellant, defendant below, contends that the bondholders referred to in the stipulation of facts had the right to receive the stock so issued in consideration for their bonds; that such bondholders transferred legal title to, or their rights to receive legal title to, or such stock to their newly created trustees, also referred to in the stipulation of facts; and that such transaction constitutes a taxable transfer.

The court sustained the appellee's motion for judgment on the basis of its contentions, concluded that no findings of fact or conclusions of law were necessary, and ordered that judgment be entered in favor of the appellee, plaintiff below, in the sum of \$2615.04, with interests and costs. (R. 49.)

The evidence (R. 1-48), none of which is disputed, discloses that the bondholders of the Pacific States

Lumber Company, under an agreement dated September 18, 1925, organized or appointed a Bondholders' Protective Committee to which they transferred, by assignment and delivery, legal title to and their respective bonds for certain subsequent transfer, or delivery, for certain purposes, reserving unto themselves ownership, or their beneficial interests therein, and accepted negotiable receipts of such committee, as evidence of such ownership or beneficial interest (R. 2-3, 13-23); that thereafter, such protective committee and such bondholders adopted and authorized the execution and carrying out of a plan and agreement of reorganization dated April 19, 1927 (R. 42-48), with the members of such protective committee as managers thereof, which the stockholders of, and the Pacific States Lumber Company in September, 1927, became a party to and agreed to carry out (R. 5); that such protective committee on January 27, 1928, requested the Pacific States Lumber Company to complete its reorganization and on that date such corporation authorized and directed its officers to complete the same; that on February 15, 1928, the Pacific States Lumber Company duly changed its name to Coos Bay Lumber Company; that on February 23, 1928, such protective committee, such managers of the plan and agreement of reorganization, and the trustees, the membership of each being the same identical persons, appointed by such bondholders, or their representatives, entered into a stock trust agreement (R. 24-32); that on or about February 25, 1928, such protective committee transferred or delivered the bonds held by them to the Coos Bay Lumber Company which on that

date issued and delivered to such trustees legal title to and 63,757 shares of its first preferred stock and 63,757 shares of its common stock, in consideration for the bonds of such bondholders, and on or about that date, said trustees, issued and delivered their trust receipts to said bondholders as evidence of said bondholders' ownership of, or beneficial interest in and to said stock; and that in addition, said corporation issued and delivered to F. A. Warner, as trustee for the former stockholders of such corporation, 10,000 shares of its second preferred stock in consideration for their surrendered and cancelled stock in accordance with said plan and agreement of reorganization to which said stockholders had become parties (R. 6), with respect to which, the appellee admits the tax paid on such transfer in the amount of \$200 under the provisions of the identical statute was legally assessed and collected. (R. 10, 36-37.)

In other words, the evidence conclusively shows that the bondholders purchased and paid for the stock issued by assignment and delivery of their bonds and that the trustees received and held legal title to and the shares of stock so issued, which the trust receipts show the real or beneficial ownership of to be vested in the bondholders and not the trustees.

The only inference of fact or conclusion of law that may be fairly drawn from such evidence is that the trustees obtained the right to receive legal title to and the shares of stock issued from the bondholders who paid the consideration therefor by assignment in blank and delivery of their bonds, or that the bondholders,

by execution of certain agreements and plan of reorganization, thereby transferred to their trustees, or nominees, legal title to, or their respective rights to subscribe for, or to receive legal title to, and the actual shares of stock issued by appellee direct to such trustees in consideration for the bonds of such bondholders. Any inference of fact, or conclusion of law to the contrary, is in direct opposition to the evidence and would, of course, have nothing to sustain it. The appellee, in effect, concedes these statements to be accurate with respect to the like transfer by the former stockholders effected upon the issuance of the 10,000 shares of its second preferred stock to the trustee for such former stockholders of appellee corporation as a part of the same transaction. (R. 10, 36-37.)

The respective rights of the bondholders to receive the consideration paid, namely the stock issued, for their bonds are inherent rights incident to and coextensive with their respective rights of ownership of said bonds whether they hold legal title thereto themselves, or possess negotiable trust receipts representing or evidencing such ownership.

If the right to receive legal title to and the stock issued by appellee in consideration for their bonds was not inherent in such bondholders but rested solely with the newly created trustees, then no necessity existed for the agreements dated September 18, 1925 (R. 13-23), April 19, 1927 (R. 44-48), May 4, 1927 (R. 42-43), and February 23, 1928 (R. 24-32), and the appellee is in error with respect to the \$200 item of the total tax assessed and paid which it concedes was legally

assessed and collected on a part of the same transaction.

With the burden of proof resting squarely upon the appellee, plaintiff below, it made no attempt and has completely failed to show by the evidence just how such right to receive arose in the trustees appointed by the bondholders, or their representatives, or from whom they obtained it, or explain just why the appellee issued the stock to the trustees, or for what consideration flowing from them; consequently the record contains neither any sufficient nor any substantial evidence to sustain the judgment.

Section 800 and Schedule A-3, Title VIII, of the Revenue Act of 1926, clearly provide that the tax of 2 cents per share is imposed on all sales, or agreements to sell, or memoranda of sales, or deliveries, or transfers of legal title to shares or certificates of stock, or of profits or interest in property or accumulations in any corporation, or to rights to subscribe for or to receive such shares or certificates (*Travis v. Ann Arbor Co.*, 168 N. Y. Supp. 53, affirmed on appeal, 227 N. Y. 640; *George A. Hormel & Co. v. United States*, 10 Fed. Supp. 623 (Minn.)), and it is elemental that one cannot read into the statute any exceptions or exemptions merely because the transfers may be termed technical or formal. (*George A. Hormel & Co. v. United States*, *supra*.) This is particularly true when it is considered that the statute applies to all transfers of every kind or character. Consequently it makes no difference whether the transfers are made to an employee, nominee, agent, transfer agent, trustee, voting

trustee, legatee, or stockholder, except that the transfer to the stockholder, like that of an outright purchaser, covers not only legal title but the beneficial interest as well, and the method or medium employed in effecting the transfer is not the determining factor.

In the instant case the bondholders owned, furnished and, through their protective committee, delivered and paid the consideration for the stock issued by appellee to their newly created or authorized trustees. Hence, such bondholders, not their trustees, were legally entitled by reason of such ownership and their inherent rights coextensive therewith, to receive legal title to and such stock upon issuance. *Rockefeller v. United States*, 257 U. S. 176; *Stange v. United States*, 68 C. Cls. 395, affirmed, 282 U. S. 270; *Rensselaer & S. R. Co. v. Irwin*, 249 Fed. 726 (C. C. A. 2d), certiorari denied, 246 U. S. 671; *Marconi Wireless Telegraph Co. v. Duffy*, 273 Fed. 197 (N. J.); *United States v. Brown Fence & Wire Co.*, 9 Fed. Supp. 1008 (N. D. Ohio); *Consolidated Equities v. White*, 9 Fed. Supp. 145 (Mass.); *Raybestos-Manhattan v. United States*, 10 Fed. Supp. 130 (C. Cls.), certiorari granted, May 20, 1935; *George A. Hormel & Co. v. United States*, 10 Fed. Supp. 623 (Minn.); however, such bondholders having by their agreements dated September 18, 1925 (R. 13-23), April 19, 1927 (R. 44-48); May 4, 1927 (R. 42-43), and February 23, 1928 (R. 24-32) agreed, authorized, and directed that the stock, to be issued in consideration for their bonds, be issued direct to their trustees, they thereby transferred to their trustees legal title to, or their respective rights

to receive legal title to and such shares or certificates of stock upon issuance, without transferring ownership thereof, which is now represented or evidenced by trust receipts, therefor, thus incurring the tax liability imposed by Section 800 and Schedule A-3, Title VIII, of the Revenue Act of 1926, and Treasury Regulations 71 duly promulgated thereunder. The appellee concedes the foregoing as applied to the issuance of the 10,000 shares of second preferred stock to the trustee for the former stockholders of Pacific States Lumber Company, and such inference of fact or conclusion of law is fully supported by the cases hereinbefore cited, and the decision rendered on September 10, 1935, in the case of *Founders General Corp. v. Hoey* (S. D. N. Y.), not yet officially reported but found in Vol. I, Prentice-Hall, 1935, p. 1980, wherein the court expressly held that the tax could be sustained "on the theory that the nomination of Benton & Company as the person to whom the certificate was to be issued, falls within the exact letter of the statute taxing 'transfers of legal title to * * * rights * * * to receive such shares or certificates' ", which is tantamount to holding that the transaction involved constituted a "transfer of the right to receive legal title to, or the actual shares or certificates" and not an outright "transfer of legal title" by execution of a written assignment.

The appellee on appeal will doubtless rely on the cases of *Minnesota Mining & Mfg. Co. v. Willcuts*, 2 Fed. Supp. 789 (Minn.); *Shreveport-El Dorado Pipe Line Co. v. McGraw*, 63 F. (2d) 202 (C. C. A. 5th);

Union Trust Co. v. Heiner, 26 F. (2d) 391 (W. D. Pa.); and *Westmoreland Coal Co. v. MacLaughlin*, 8 Fed. Supp. 963 (W. D. Pa.), affirmed, *per curiam*, 73 F. (2d) 1004 (C. C. A. 3d).

With respect to all of these decisions the records made did not warrant a review except in the *Westmoreland Coal Co.* case. However, the court in each of these cases not only failed to recognize the substantial difference and distinction existing between a person or corporation as the owner of property, and the trustees, nominees, or stockholders, to whom the stock was issued direct, in consideration for property or money paid by such person, or corporation, therefor (*Gibbons v. Mahon*, 136 U. S. 549; *Van Allen v. The Assessors*, 3 Wall. 573; *The Delaware Railroad Tax*, 18 Wall. 206, 230; *Tennessee v. Whitworth*, 117 U. S. 129, 136; *New Orleans v. Houston*, 119 U. S. 265, 277), but after finding facts which are in substance and effect in harmony with the findings presented in the case of *Marconi Wireless Telegraph Co. v. Duffy*, *supra*, and the cases hereinbefore cited, reached an erroneous conclusion of law as did the District Court in the instant case and no conflict in Circuit Court decisions existed at the time to warrant application for certiorari in the *Westmoreland Coal Co.* case.

Thus it is seen that the transactions involved constitute taxable transfers by the bondholders of Pacific States Lumber Company to their trustees, or nominees, of legal title to, or their respective rights to subscribe for, or to receive legal title to, and the 127,514 shares of first preferred and common stock issued

direct by the Coos Bay Lumber Company to their trustees, or nominees, in conformity with the agreements and plan of reorganization, in consideration for such bondholders' bonds within the meaning of the provisions of the above statute and regulations.

CONCLUSION.

It is urged that the judgment and conclusions of law of the District Court be reversed, and that this case be remanded to such court, with instructions to enter specific conclusions of law and judgment in favor of the appellant herein.

Dated, San Francisco,
November 1, 1935.

Respectfully submitted,

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(Appendix Follows.)

Appendix.

Appendix

STATUTES INVOLVED.

Revenue Act of 1926, c. 27, 44 Stat. 9:

TITLE VIII.—STAMP TAXES.

Sec. 800. On and after the expiration of thirty days after the enactment of this Act there shall be levied, collected, and paid, for and in respect of the several bonds, debentures, or certificates of stock and of indebtedness, and other documents, instruments, matters, and things mentioned and described in Schedule A of this title, or for or in respect of the vellum, parchment, or paper upon which such instruments, matters, or things, or any of them, are written or printed, by any person who makes, signs, issues, sells, removes, consigns, or ships the same, or for whose use or benefit the same are made, signed, issued, sold, removed, consigned, or shipped, the several taxes specified in such schedule. The taxes imposed by this section shall, in the case of any article upon which a corresponding stamp tax is now imposed by law, be in lieu of such tax. (U. S. C. App. Title 26, Sec. 901.)

SCHEDULE A.—STAMP TAXES.

3. Capital stock, sales or transfers: On all sides, or agreements to sell, or memoranda of sales or deliveries of, or transfers of legal title to shares or certificates of stock or of profits or of interest in property or accumulations in any corporation, or to rights to subscribe for or to receive such shares or certifi-

cates, whether made upon or shown by the books of the corporation, or by any assignment in blank, or by any delivery, or by any paper or agreement or memorandum or other evidence of transfer or sale, whether entitling the holder in any manner to the benefit of such stock, interest, or rights, or not, on each \$100 of face value or fraction thereof, 2 cents, and where such shares are without par or face value, the tax shall be 2 cents on the transfer or sale or agreement to sell on each share: PROVIDED, That it is not intended by this title to impose a tax upon an agreement evidencing a deposit of certificates as collateral security for money loaned thereon, which certificates are not actually sold, nor upon the delivery or transfer for such purpose of certificates so deposited, nor upon mere loans of stock nor upon the return of stock so loaned: PROVIDED FURTHER, That the tax shall not be imposed upon deliveries or transfers to a broker for sale, nor upon deliveries or transfers by a broker to a customer for whom and upon whose order he has purchased same, but such deliveries or transfers shall be accompanied by a certificate setting forth the facts; PROVIDED FURTHER, That in case of sale where the evidence of transfer is shown only by the books of the corporation the stamp shall be placed upon such books; and where the change of ownership is by transfer of the certificate the stamp shall be placed upon the certificate; and in cases of an agreement to sell or where the transfer is by delivery of the certificate assigned in blank there shall be made and delivered by the seller to the buyer a bill or memorandum of such sale, to which the stamp shall be affixed; and every bill or

memorandum of sale or agreement to sell before mentioned shall show the date thereof, the name of the seller, the amount of the sale, and the matter or thing to which it refers. Any person liable to pay the tax as herein provided, or anyone who acts in the matter as agent or broker for such person, who makes any such sale, or who in pursuance of any such sale delivers any certificate or evidence of the sale of any stock, interest or right, or bill or memorandum thereof, as herein required, without having the proper stamps affixed thereto, with intent to evade the foregoing provisions, shall be deemed guilty of a misdemeanor, and upon conviction thereof shall pay a fine of not exceeding \$1000, or be imprisoned not more than six months, or both. (U. S. C. App., Title 26, Sec. 901.)

REGULATIONS INVOLVED.

Treasury Regulations 71, approved July 7, 1928, promulgated under the Revenue Act of 1926:

Art. 31. Basis of Tax.—Every transfer or sale of stock, either before or after issuance of a certificate, is taxable. The tax accrues at time of making the sale or agreement to sell or memorandum of sale, or delivery of, or transfer of the legal title to shares, or certificates of stock, or of profits, or of interest in property or accumulations in any corporation, joint-stock company, or association, or of the right to subscribe for or to receive such shares or certificates, regardless of the time or manner of the delivery of the certificate or agreement or memorandum of sale.

Art. 32. Rate of Taxation.—(a) In the case of stock having a par or face value, the amount of the tax is 2 cents on each \$100 or fraction thereof of the total par or face value of the shares or certificates involved in the sale or agreement to sell, whether such aggregate par or face value is greater or less than \$100; e. g., where the total par or face of the shares involved in the transaction is \$100 or less, the tax is 2 cents; where such value is in excess of \$100, the tax is 2 cents on each \$100 or fraction thereof.

(b) In the case of shares of stock without par or face value, the tax is 2 cents on the transfer or sale of, or agreement to sell, each share.

Art. 33. Computation of the Tax.—(a) In the case of stock having a par or face value, the amount of the tax is computed upon the total par or face value of the shares and not upon the amount that may have been paid in on such stock; e. g., where stock of the par value of \$100 is sold, for which only \$25 is paid, the tax is reckoned upon the par value of \$100 and not upon the \$25 paid.

(b) Where one certificate represents several shares (however large the number of shares) on the transfer of such certificate the tax is computed upon its face value and not on the face value of each separate share of stock, or of profits, or of interest in property or accumulations; e. g., on the transfer of one certificate representing 500 shares, par value \$5, the face value of the certificate being \$2500, the stamp tax is 50 cents.

(c) In the case of stock without par or face value, the tax is computed on each share; e. g., the tax on the transfer of a certificate for 20 shares of such stock is 40 cents.

Art. 34. Sales and Transfers Subject to Tax.—The following transactions are subject to the tax:

(a) The sale, or transfer, or change of ownership, of certificates of stock, or of profits, or of interest in property or accumulations in corporations, joint-stock companies, or associations.

(b) The sale or transfer of shares of stock, whether or not represented by certificates.

(c) The transfer of stock to or by trustees.

(d) The transfer of voting trust certificates.

(e) The sale or transfer of temporary or interim certificates of stock.

(f) The sale or transfer of certificates or shares representing beneficial interests in an association. See article 77 (1) (e)—“Association”.

(g) The transfer of the interest of a subscriber for stock, however such interest may be evidenced or conditioned upon further payments.

(h) The transfer of the right to subscribe for stock in any corporation, joint-stock company, or association, whether or not evidenced by warrants.

(i) The transfer of the right to receive a stock dividend already declared.

(j) The transfer or surrender of stock to a corporation, for the purpose of the corporation, whether or not it intends eventually to sell such stock.

(k) The sale of or agreement to sell shares of stocks made by a broker, directly or indirectly, for himself.

(l) The sale or transfer of stock by a broker at a price different from that at which he accounts to his selling customer.

(m) The transfer of stock in pursuance of a gift, bequest, or conveyance by trustees.

(n) The transfer of stock from parties occupying fiduciary relations to those for whom they hold stock.

(o) The transfer of certificates of stock by an administrator or executor to the legatee or distributee.

(p) The transfer of stock on the books of a domestic corporation, regardless of where the sale is made or the stock certificates delivered.

(q) The sale, transfer, or delivery, within the territorial jurisdiction of the United States, of shares of stock of a foreign corporation.

(r) The transfer of stock of a corporation to be merged to the merging corporation prior to the actual merging and as a condition precedent to the merger.

(s) Upon a merger, the transfer of stock owned by a corporation which is merged into another corporation from the name of the first to the name of the second corporation is a transfer by the act of the parties, and not wholly by operation of law.

(t) The transfer of the right to receive stock which a corporation has unconditionally agreed to issue.

(u) Transfers of stock are subject to the tax even though the holders thereof are not entitled in any manner to the benefit of the stock.

(v) Transfer of stock from old firm to new firm succeeding to its business where personnel is different.

(w) Transfer of stock from a firm to individual members thereof upon dissolution of the business.

United States
Circuit Court of Appeals

For the Ninth Circuit.

JOHN P. McLAUGHLIN, as United States
Collector of Internal Revenue, First
District of California,

Appellant,

VS.

COOS BAY LUMBER COMPANY,
a corporation,

Appellee.

BRIEF FOR APPELLEE.

LYMAN HENRY,

Merchants Exchange Building,
San Francisco, California,

Attorney for Appellee.

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Here the bondholders of the Coos Bay Lumber Company were acting as individuals unencumbered by any rule of law requiring a corporation transferring all of its assets to receive in itself the consideration therefor.

The former bondholders received the voting trust certificates or exactly the thing of value for which they contracted. The certificates of stock and legal title thereto were issued originally to and held only by the voting trustees who were the same persons who formerly held legal title to the bonds, i. e., the Bondholders' Protective Committee

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United States
Circuit Court of Appeals
For the Ninth Circuit.

JOHN P. McLAUGHLIN, as United States
Collector of Internal Revenue, First
District of California,

Appellant,

vs.

COOS BAY LUMBER COMPANY,
a corporation,

Appellee.

BRIEF FOR APPELLEE.

I.

Corrected statement of case and exposure of appellant's unfair and unjustified initial argument that the stipulated facts do not support the judgment.

Beginning on page 3 of appellant's brief, hereinafter referred to as the "Government's brief", a somewhat detailed review is made of the transaction involved in the issuance of the stock in question with, however, the omission of an important agreed and stipulated fact, namely,

That the reorganization plan provided not that the bondholders' committee should receive the issue of stock from the plaintiff corporation but that the stock should be issued directly to and held only by voting trustees named by the investment bankers pursuant to said plan.

This is the allegation of paragraph V of the complaint (R. 3) as amended and stipulated to by agreed amendment and stipulation paragraph 3 (R. 40). This above mentioned amendment and stipulation in this regard reads as follows:

“And except as so amended the allegations of paragraphs V and VIII (of the complaint) are true.”
(R. 40.)

The amendment of the complaint as thereinbefore in this paragraph 3 (R. 40) stated, amended the error of the complaint in stating the manner of selecting the voting trustees and is not important and does not affect the basic question involved in this appeal. The amendment was that the trustees were named by the investment bankers and not by the bondholders—an immaterial error also made by the Government's brief, page 8.

We thus see that this corrected statement of facts eliminates the necessity of further answering the “shabby” attempt on the part of the Government as set forth at pages 12, 13, and 14 of its brief to argue that the agreed statement of facts does not support the judgment. The writer of this brief describes this argument of the Government as “shabby” advisedly.

There was no dispute when the case was tried in the court below as to the facts involved and both counsel for

the plaintiff and the defendant there properly considered the stipulated facts as presenting the question and issue discussed in the Government's brief following the italicized title at page 14. On page 15 of this portion of its brief it is admitted that there is no dispute on the facts.

The Government's own Bill of Exceptions and Assignment of Errors show that the only issue before this Court is one of law, namely, whether as a matter of law it can be said that there was a transfer of a right to receive stock where the stock was to be and was issued directly to and held only by the trustees. The Bill of Exceptions in this regard states:

"The defendant moved for judgment in his favor, and further moved the Court to conclude from the stipulated facts that *as a matter of law** the bondholders referred to in said Stipulation of Facts had a right to receive the stock issued in consideration for their bonds and transferred to the newly created trustees such right, and that said transaction constituted a taxable transaction." (R. 52.)

Paragraphs III and V (R. 56-57) of the Government's Assignment of Errors repeat this language of the Bill of Exceptions and confirm the fact that the only issue before this Court is one of law as to whether or not the Court can say that as a matter of law there was a transfer of the right to receive stock under the stipulated facts that the stock was "to be issued directly to and held only by voting trustees."

*Emphasis and italics throughout this brief are supplied.

If the Government in such tax cases were permitted to “run out” on its stipulations of fact, counsel in these tax cases (which present simply questions of law which both parties desire to be presented with the minimum expense and trouble) would be loathe to accept such stipulations of fact and would require a full and complete trial with its incident burden and expense in every case.

It is rather amazing that the Government which made no request for findings of fact should be contending that the agreed statement of facts does not constitute the findings of fact of the Court. This Court has held that the submission of a case on agreed statement of facts is a sufficient stipulation for waiver of jury and “that the agreed statement is in the nature of a special verdict, and that on writ of error the Court will consider the sufficiency of the agreed statement to support the judgment.” *Greer-Robbins Co. v. United States*, 19 Fed. (2d) 841-842. The statement in the Minute Order for Judgment by the trial court (R. 49) that “the case having been submitted on stipulated facts, no findings of fact or conclusion of law are necessary” can have no other meaning than that the Court in effect adopted the stipulated facts as its findings of fact. We have pointed out that the stipulated fact “that the stock was to be issued directly to and held only by the voting trustees,” is sufficient to sustain the judgment.

We ask, therefore, that the Court dismiss as improper and ignore that portion of the Government’s brief, pages 12, 13 and 14 which in effect attempts to repudiate the agreed statement of facts presenting, and accepted by counsel and the court below as presenting, the issues in-

volved in the remaining portion of the Government's brief, i.e., pages 14 to 23.

So that the Court might have a little more complete picture of the background of the facts under which the taxes sued for were collected, we might mention here that the additional assessment, for which the taxpayer obtained judgment of refund in the court below, occurred in connection with the taxpayer's claim for refund of the amount of original issue stamps erroneously fixed to the no par value common stock of the Coos Bay Lumber Company and to the second preferred stock. The taxpayer's position under the claim for refund was allowed by the Government but the Government for the first time, more than two years after the reorganization had been completed, invoked the theory involved in the present case to the effect that the bondholders had in legal effect transferred the right to receive the stock which was issued to the voting trustees although the plan of reorganization, as noted above, provided that the stock be issued directly to said voting trustees. The full account of this original claim for refund by the taxpayer is given in paragraphs X to XVII (R. 6 to 11) as admitted by answer paragraphs IX to XIII (R. 36-37).

II.

Brief Summary of facts and question presented.

Where the bondholders of a corporation surrender their bonds to the corporation issuing certain shares of stock directly to designated trustees with no right in a non-consenting bondholder to cause the stock to be issued to himself, is there a transfer of the legal title to a right to receive the stock which is subject to the federal transfer stamp tax act imposing a tax liability on the transfer of legal title to shares of stock or of the right to receive same? In other words, under such circumstances is there in contemplation of law the transfer of a right to receive stock which the bondholder never had?

The doctrine that there can be a transfer of the legal title to a right to receive stock **IN CONTEMPLATION OF LAW** where there is no such right in fact is confined to the situation where the party furnishing the consideration for the issuance of stock to a third person is **A CORPORATION** transferring its assets upon which the law imposes the obligation in the first instance to receive the stock.

Here the bondholders of the Coos Bay Lumber Company were acting as individuals unencumbered by any rule of law requiring a corporation transferring all of its assets to receive in itself the consideration therefor.

The former bondholders received the voting trust certificates or exactly the thing of value for which they contracted. The certificates of stock and legal title thereto were issued originally to and held only by the voting trustees who were the same persons who formerly held legal title to the bonds, i. e., the **Bondholders' Protective Committee**.

The facts involved in the present case may be summarized as follows: Outstanding bonds of the Coos Bay Lumber Company had come into possession of a bond-

holders' committee. The latter entered into a reorganization agreement with the Coos Bay Lumber Company which provided that the Company would issue its first preferred and common stock directly to a group of trustees for the former bondholders (which trustees were the same persons constituting the bondholders' committee) in consideration of the surrender by the committee to the Company of the bonds held by it and issuance by the trustees of voting trust certificates to the former bondholders. There was in fact no time when any persons, other than the trustees, had a right to receive this issue of stock.

This case as all tax cases must be approached with the familiar rule of judicial construction of such taxing statutes, namely, that they must be construed liberally in favor of the taxpayer and if there is a doubt in the meaning of the statute that doubt must be resolved against the Government and in favor of the taxpayer. *Burnett v. Niagara Falls Brewing Company*, 282 U. S. 648, at 654; *U. S. v. Merriam*, 263 U. S. 179 at 187-188.

The pertinent portion of the taxing statute in question imposes a stamp tax liability "on transfers of legal title to shares or certificates of stock, or to rights to subscribe for or to receive such shares or certificates" (26 U. S. C. A., Section 901 Schedule A—appendix Government's brief page i). Accordingly there must have been a transfer of legal title to shares or a transfer of the right to receive the same for the Government to sustain its position. The statute is so clear in this regard it is not even necessary to resort to the above mentioned rule of construction against the Government to support our case.

Since the filing of the Government's brief, the United States Supreme Court has decided the case of *United States v. Raybestos-Manhattan, Inc.* under writ of certiorari granted May 20, 1935. The Court of Claims decision in this case is cited in the Government's brief at page 20 along with a number of other cases. The Supreme Court decision was rendered on November 11, 1935, opinion by Mr. Justice Stone. The case may be found in the issue of the "United States Law Week" for November 12, 1935, page 29.

In this *Raybestos-Manhattan case* there was a consolidation or merger under the laws of New Jersey whereby the Raybestos-Manhattan Company, a New Jersey corporation, acquired all of the assets of the Raybestos Company, a Connecticut corporation and the United States Asbestos Company, a Pennsylvania corporation, in consideration whereof the New Jersey corporation issued an agreed number of its shares of stock to the stockholders of the old Connecticut and Pennsylvania corporations. Despite the provision in the contract of merger that the New Jersey corporation would deliver "to the Connecticut Company (likewise to the Pennsylvania Company) *or its order*" the required number of shares of stock, Mr. Justice Stone stated as follows:

"The government and the taxpayer are not in accord as to the precise interpretation to be placed upon the contracts which resulted in the consolidation, but accepting the taxpayer's contention for purposes of decision, we assume that it was agreed by all concerned that the shares of petitioner were to be issued directly to the stockholders of the two

corporations without further intervention by the latter.”

We must keep in mind, however, in the consideration of this *Raybestos case* decision by the Supreme Court that it is confined solely to the facts there involved, namely, to a situation where an old *corporation* transfers all of its assets to a new corporation in consideration of issuance of shares from the new corporation to the stockholders of the old **without anything of value such as voting trust certificates given to the old corporation.** When we realize that the party furnishing the consideration, that is the old corporation, was in contemplation of law required to receive in itself the consideration for a transfer of its assets, the case is readily distinguishable from the case at bar. That the Supreme Court had in mind this distinction is clearly shown in the following statements in the opinion:

“The new shares could not lawfully be issued to any other than the grantor corporation without its authority, and that authority could not be exercised for the benefit of third persons other than its own assenting stockholders. * * *

It (the statute) embraces the more general one, inseparable from the transaction by which the obligation to issue the stock was created and *which inhered in the two corporations by operation of law.*”

In the case of the Coos Bay Lumber Company, the bondholders could do anything they wanted to with the bonds. The bonds were simply like money which could be used to buy stock to be issued to the persons designated.

The fact that the bondholders were asked to indicate their assent to the contemplated stock issue did not give them, themselves, the right to receive the certificates. The plan of reorganization expressly provided to the contrary. Under the plan of reorganization all the dissenting bondholder could do was to "withdraw (his) bonds on the terms stated in the Deposit Agreement" (R. 43). The terms stated in the Deposit Agreement for the withdrawal of the bonds were simply that the withdrawing or dissenting bondholder pay the pro rata share of the expenses of the Bondholders' Protective Committee already incurred (Paragraphs Fourth and Second of Deposit Agreement, Exhibit "A", R. 20 and 17, respectively). Any of the first preferred and common stock not so issued to the trustees under the plan was to be cancelled. (Plan and agreement paragraph 2—R. 44—Government Brief, p. 7.) It can not be said, therefore, that the bondholders had any right to have the certificates of stock issued to themselves when the plan of reorganization expressly denied this right.

In the *Raybestos case* it may be admitted that the issuance of stock to the stockholders of the old corporation was a mere short cut. It cannot be successfully contended, however, that the issuance of the stock to the voting trustees in the case of the Coos Bay Lumber Company was such a mere short cut. It was an essential part of the reorganization scheme. *We cannot ignore that the reorganization contracts and particularly the stock trust agreement Exhibit "B" (R. 24) show that the very nature of the transaction was to maintain control of the affairs of the corporation through election of directors by others than the former bondholders.* This agreement

provided that the stock would not be delivered to the holder of the voting trust certificate unless at least seventy-five per cent in aggregate value of holders of said trust receipts so requested. The stock was so tied up until January 1, 1932, or approximately four years after the consummation of the plan.

The situation is in effect no different from that in which a father, desirous of making a gift to his son, takes \$1,000.00 of his own cash to a corporation, pays it over the counter and has a certificate of stock issued to his son. We do not believe that the Government will contend that the recent decision of the Supreme Court in the *Raybestos case*, supra, can be extended to impose not only an original issue stamp tax upon such a purchase by a father but also a transfer stamp tax upon the imaginary transfer of a right to receive stock in the father which never existed. As a matter of fact, even at a time when the Bureau of Internal Revenue was insisting that an obligation for transfer stamp taxes arose in the old and new corporations setup, like the *Raybestos case*, the Bureau did not contend that there would be a tax in such father and son transaction.

We quote the following report from O. D. 176, 10-21-320 S. T.:

“A conveyed to a corporation several parcels of real estate which he owned individually. The corporation was capitalized for \$500,000, the same being represented by 5,000 shares of no par value stock, of which 1000 shares were issued to each of his five children. Held that since there was no privity of contract between A and his children, and under the terms of the contract which A had with the corpora-

tion the stock was in the first instance to be issued to the children, hence A had at no time any right to receive such stock, and therefore could make no taxable transfer of such right."

Until the decision by the Supreme Court in the *Raybestos case*, supra, in the great majority of cases, the lower courts (where there was this new and old corporation merger transaction whereby the assets of an old corporation were transferred to a new corporation and the stock was eventually acquired by the stockholders of the old corporation) had refused to find a transfer unless the agreement between the old and the new corporation or the agreement of reorganization and merger expressly gave the power to the old corporation itself to cause the certificates first to be issued to it. As a matter of fact even the contract of reorganization in the *Raybestos case*, as quoted in the opinion of the court below, apparently gave to the old corporation the right to direct whether the stock should be delivered to the old corporation or to its order, i. e., its stockholders. Quoting from the opinion of the court below in this *Raybestos case* we find the following statement in this connection:

"The selling corporation (the old corporations) were the ones who had the right to receive the consideration (stock) for their assets and business sold to plaintiff (the new corporation) and these (old) corporations, when they transferred their assets to plaintiff, directed that the stock of the plaintiff be delivered 'to the Company or upon its order'." (10 F. Supp. 130, 136.)

There is only one corporation involved in the present reorganization or transaction, namely, the Coos Bay Lum-

ber Company. Its name before the reorganization was Pacific States Lumber Company. By the change of name and increase of the authorized capital stock to permit the exchange for the bonds there was simply a continuation of the old company. This, of course, is not contested by the Government. The bonds were surrendered to the same company which was the obligor under the bonds and the same persons who had constituted the bondholders' committee holding legal title to the bonds received the legal title to the shares of stock issued in exchange.

Even if there were a concept of law requiring former bondholders, who have retained simply an equitable interest in their bonds deposited with a committee, to receive something of value in exchange for the surrender of the bonds, this has been accomplished in the Coos Bay Lumber Company's case. The former bondholders received voting trust certificates which admittedly were things of value. The Bondholders' Protective Committee which held legal title to the bonds became the voting trustees to whom the certificates of stock were issued. In a very real and practical sense, as noted above, the bondholders' committee, continuing as voting trustees, maintained the desired control of the Company.

III.

At the time the bonds were deposited and also at the time the stock was issued there was no transfer stamp tax on the transfer of bonds. There was no such tax until the Revenue Act of 1932. The Government cannot justify its position by reason of the fact that the law designedly omitted taxing transfers of bonds.

The agreed statement of facts shows that the bonds were deposited with the Bondholders Protective Committee giving to the committee legal title to the bonds under agreement dated September 18, 1925 (R.—Exhibit “A”—13 et seq.). At this time (Sept. 18, 1925) there was no plan of reorganization or issuance of stock under way. Certainly at this date the Government does not seek to justify the arbitrary assessment that the taxpayer is suing to recover because the law itself did not then provide for a stamp tax liability on a transfer of bonds. Yet we may hazard a doubt that this assessment would have been made had there been a transfer tax liability on bonds at the time. Certainly there were enough taxable transactions which were created or made possible to rebut any idea that the Government was being defrauded of revenue. When the stock was issued, original issue stamps were paid; upon transfer of voting trust certificates, transfer stamps were imposed; if the trustees had been changed, transfer stamps on the transfer of the stock to new trustees would have been affixed; when the trust was terminated, transfer stamps on the transfer of the stock to the holders of the voting trust certificates were imposed. Under such circumstances it can hardly be said that there is any justification in public policy in creating as a matter of law a fictitious transfer of a non-existent right to receive stock in order to increase revenue.

IV.

Discussion of two cases decided the same day by District Court in Massachusetts illustrating the difference between the situation where a reorganization is effected of an old corporation whereby the stock of a new corporation is issued to the stockholders of the old corporation, in which case the Supreme Court has recently held a taxable transfer occurs, and the situation presented in the present case where only one corporation is involved and the parties furnishing the consideration for the issuance of stock to others acquired voting trust certificates.

The Government's brief cited no cases, and we know of none, which have imposed a double stamp tax liability because of a transfer found to exist as a matter of law in any other situation except that of an old and new corporation setup as found in the *Raybestos* case. Furthermore at least one decided case (*Consolidated Equities, Inc. v. White*—discussed infra) has very definitely refused to find a transfer of a right to receive stock as a matter of law where none existed in fact in a transaction involving none of the limitations imposed by the concept of law that a corporation surrendering its assets must receive the consideration therefor. On June 17, 1934, Judge Brewster for the United States District Court of Massachusetts decided two cases which very pointedly illustrate and support the position taken by the Coos Bay Lumber Company. These two cases have the same title and were decided the same day, although reported in different volumes of the Federal Reporter. *Consolidated Equities, Inc. v. White*, 7 Fed. Supp. 851 and *Consolidated Equities, Inc. v. White*, 9 Fed. Supp. 145 which, for convenience, we refer to, respectively, as The Voting Trust Case and The Old and New Corporation Case.

In the Voting Trust Case, 7 Fed. Supp. 851, brokers offered for sale at a stated price trust certificates representing shares in an investment corporation. A customer electing to purchase sent the purchase price to the broker who in turn paid it to the corporation, *whereupon the corporation issued shares to voting trustees* who thereupon instructed the transfer agent of the corporation and of the voting trust to issue to the purchaser voting trust certificates for the number of shares purchased and paid for. Original issue stamps were admittedly paid and due on the issue to the voting trustees but the taxpayer corporation contended that no *transfer* stamps were due since the person furnishing the consideration for the issuance of the stock never had the right to receive the stock or the certificates which were issued to the voting trustees and hence transferred nothing to them. The Court upheld the taxpayer's contention saying:

“It is obvious that what the customer of the broker purchased and what he received was a certificate representing a beneficial interest in stock which had been originally issued to voting trustees to hold for the benefit of the subscriber. This transaction involved no transfer of legal title to the shares, nor to any right to such legal title either from purchasers to trustees or from trustees to purchasers. If the theory of the government that the purchaser became a shareholder by virtue of his payment to the broker of the purchase price be adopted, the voting trustees held the stock for the sole benefit of the purchaser and purchasers' interest was represented, and intended to be represented, by the voting trust certificate. *No transfer actual or constructive, from the purchaser was necessary to vest the legal title in the voting*

trustees. Union Trust Co. of Pittsburgh v. Heiner, 26 F. (2d) 391." (7 F. Supp. 851.)

This is exactly the situation involved in the Coos Bay Lumber Company's transaction. The bondholders, instead of using money to obtain the issuance of stock to voting trustees and obtain the voting trust certificates, used their bonds as the purchase price. All that they received and all that they ever had a right to receive was the voting trust certificates. As noted before in this brief the plan of reorganization under which the stock was issued gave no option to the bondholder whether he would have the stock issued to himself or to voting trustees but his only option was to consent to have the stock issued to the voting trustees and accept the voting trust certificate or withdraw his bonds. In other words, he could either purchase the voting trust certificates or keep his money (bonds) (R. 43).

On the same day in the Old and New Corporation case, 9 F. Supp. 145, Judge Brewster held that where a new corporation is formed, pursuant to a plan for a consolidation of three old corporations and the stock of the new corporation was issued directly to the stockholders of the old corporations, both original issue stamps and transfer stamps should be affixed. While the plan of reorganization indicated that the old corporations had expressly been given the power to direct whether they would in the first instance receive the stock, Judge Brewster in his opinion went further and indicated the same position taken by Mr. Justice Stone when he said:

"The plaintiff issued its shares under the laws of Massachusetts which require all issued stock to be

paid for in cash, property or services. It is clear that plaintiff's stock was to be paid for, not in stock of the old corporations, but in the assets of those corporations. It follows that the corporations, and not their stockholders, were in the first instance entitled to the stock of the new corporation. If the stockholders became entitled to this stock, it was because by votes of the old corporations the right to receive the stock shifted from the corporations to their respective stockholders. Was this a transfer, taxable under Title VIII, Schedule A(3) of the Revenue Act of 1926?

“The plan of consolidation *in legal contemplation* involved an exchange of assets for capital stock and a distribution in liquidation among the stockholders of the old companies of the new stock thus acquired. To accomplish this end, the old corporations took a short cut by directing the new corporation (the plaintiff) to issue the stock directly to the stockholders of the old corporations in the same proportions as would have obtained if the old corporations had made the liquidating distribution.” (9 F. Supp. 145 and 146.)

While Judge Brewster then indicated that a contrary result might have been reached in accordance with *Minnesota Mining & Manufacturing Company v. Willcuts*, 2 Fed. Supp. 789 and *Westmoreland Coal Co. v. MacLaughlin*, 8 F. Supp. 963, nevertheless, in view of the above quoted language it seems clear that the Court must have had in mind some concept of law requiring in legal effect that a corporation transferring its assets in consideration of the issuance of stock in a new corporation to its stockholders makes a transfer of the right to re-

ceive stock. We thus see that on the same day and by the same Judge we have decisions illustrating the difference between the Coos Bay Lumber Company's claim and the old and new corporation setup involved in the *Raybestos case*.

The Voting Trust Case, 7 Fed. Supp. 851, was appealed by the Government to the Circuit Court of Appeals but the judgment for the taxpayer was affirmed. There was no appeal in The Old Corporation New Corporation case.

The opinion of the Circuit Court of Appeals affirming this judgment in favor of the taxpayer in the Voting Trust Case is found in 78 Fed. (2d) 435. The case was not tried in the court below on stipulated facts and consequently findings of fact were necessary. However the Court on appeal sustained the lower court's finding that the purchasers bought voting trust certificates and not rights to receive stock which could be said to be transferred to the voting trustees. This, of course, was just what occurred in the case of the Coos Bay Lumber Company. As noted above, all that the bondholder could require in case he assented to the plan was the delivery of voting trust certificates for his interest as provided in the stock trust agreement Exhibit "B" (R. 24) under which agreement it was stipulated that all of the first preferred and no par value common stock was held. (Paragraph 5 of Stipulation of Facts R. 40-41.) While the Circuit Court of Appeals recognized a liberal principle in favor of the government that substance rather than form should be considered, nevertheless, the Court refused to extend the doctrine of the old corporation new corporation cases against the taxpayer. The Court said:

“It is true, as the Collector contends, that in matters of this sort the statute requires that substance rather than form shall be considered, and that ‘all transfers of legal title to shares or certificates whether technical sales or not’ are taxable; (*Provost v. U. S.*, 269 U. S. 443, 458; *Goodyear Co. v. U. S.*, 273 U. S. 100) *but this does not warrant imputing to transactions a character substantially different from what they in fact were in order to make them taxable.*” (78 Fed. (2) 436.)

We correct at this point an apparent misapprehension or mistaken reliance found in the Government’s brief regarding the issue of the 10,000 shares of second preferred stock of the Coos Bay Lumber Company in exchange for all of the former *stock* of the company. On pages 17-18 and 21 of its brief the Government argues that since the taxpayer accepted without contest the assessment of transfer stamps on this issue of second preferred stock therefore the taxpayer has in effect admitted the propriety of assessing transfer stamps on the *bond* transaction. This, of course, is an error that is easily exposed. As we have shown at the time of the transaction involved there was no statute imposing a stamp tax liability on the transfer of bonds or the right to receive the same. However, there was at all times a transfer stamp tax liability with regard to stock. Since the 10,000 shares of second preferred stock were issued to persons other than former stockholders there was in effect a transfer by the former stockholders of the shares of stock. Either it would have been necessary to affix the transfer stamps to the old shares surrendered or to the new issue. As we pointed out earlier in this

brief, the Government's position cannot be sustained on the theory that the Revenue Act at the time of the transaction involved did not cover the transfer of *bonds*.

On page 21 of the Government's brief following the erroneous analogy of the 10,000 shares of second preferred stock the Government cites the recent case of *Founders General Corp. v. Hoey*, (S. D. N. Y.) Vol. I; Prentice Hall, 1935, p. 1980. This case is clearly distinguishable from the claim of the Coos Bay Lumber Company since the Founders General Corp., there, had already *subscribed* for stock in an issuing corporation which was later to be delivered. Before delivery date, however, the Founders General Corp. designated a third party nominee to receive the stock. Obviously there was a transfer of an *existing* right to receive stock and transfer stamps were properly required. The District Court in this last mentioned case very clearly indicated that unless the taxpayer corporation had at some time possessed the right to receive stock it would not have upheld the tax, and furthermore, pointed out that even if the parties ~~have~~ accomplished the same result by a different method this would not justify the tax. The Court said:

“But the transaction as actually carried out did not take this form, although it accomplished the same result and in the matter of stamp duties the form is all important. *United States v. Isham*, 17 Wall. 496. The tax cannot therefore be sustained on the theory that in legal effect the transaction was the same as though the plaintiff had taken legal title to the shares and transferred them to its nominee. But it can be sustained, in my opinion, on the theory that the nomination of Benton & Company as the per-

son to whom the certificate was to be issued, falls within the exact letter of the statute taxing 'transfers of legal title to * * * rights * * * to receive such shares or certificates.' *Prior to such nomination the plaintiff had the right to receive the shares and by its nomination its right was transferred to its nominee.*"

We cannot believe that the Supreme Court in the *Raybestos* case intended to overrule its decision in the case of *United States v. Isham*, 17 Wall. 496, cited in the above quotation. It is one thing for the Court to hold that as a matter of law an old corporation has the right to receive in the first instance the shares of stock in a new corporation issued in exchange for its assets and then hold that in *legal effect* there has been a *formal act* permitting the imposition of an excise tax, but quite another thing to extend this doctrine to create a direct tax on the mere ownership of property. The constitutional objection of such an extension of the doctrine cannot be ignored. This constitutional objection we shall take up in the following concluding section.

V.

The Stamp Tax can be upheld only as an excise tax since it does not apply the apportionment as required in Article I, section 2, clause 3 of the Constitution of the United States.

If the stamp tax is construed to apply simply by reason of the ownership of property with the potential power to transfer stock, which power is not in fact exercised, then it becomes a direct tax upon the property itself and must fall under the constitutional objection above.

In our brief in the lower court we simply suggested that the statute if construed to apply to the situation where there has been neither a right to receive stock nor a transfer of the same, then it would be subject to grave constitutional objections. Earlier in this brief we pointed out the absurd result that would follow from the logical application of the Government's contention where a father would be subject to a transfer stamp tax simply because he owned and possessed the money which was used as consideration for the issuance of stock directly to his son. Yet on principle we fail to see any difference between this father and son relationship and the situation where bonds instead of money are used for the issuance of stock. Congress certainly cannot pass a statute directly taxing the ownership of property unless the tax is apportioned according to population. (See e. g. the historical second income tax cases *Pollock v. Farmers Loan and Trust Company, etc.*, 158 U. S. 601.)

The Supreme Court has held that such a stamp tax on a memorandum or contract of sale of a certificate of stock is an excise tax and not a direct tax. *Thomas v. U. S.*, 192 U. S. 363. In this case the Court said:

“The sale of stocks is a particular business transaction in the exercise of the privilege afforded by the laws in respect to corporations of disposing of property in the form of certificates. The stamp duty is contingent on the happening of the **event** of sale, and the element of absolute and unavoidable demand is lacking.” (192 U. S. 363, 371.)

It would seem to take little argument to show that if there has been no **“event”**, i. e., no transfer of a right to receive stock, then there has been no act or privilege which has been exercised that will justify the tax. However, if the Government arbitrarily claims that there has been a transfer of a right to receive as a matter of law where there is none in fact, then the tax becomes a direct tax upon the property itself or the individual owning the property himself and falls within the constitutional objection.

Of course we contend that the clear wording of the stamp tax statute in question imposing a stamp tax “on transfers of legal title to shares or certificates of stock * * * or to right to receive such” expressly prohibits the Government from imposing the tax in question. However, the above constitutional objection is made to show the fallacy of the Government’s argument that there can be a transfer of a right that never existed.

CONCLUSION.

In conclusion therefore we submit that the agreed statement of facts setting forth fully the transaction involved in this dispute and particularly the stipulated fact that the plan of reorganization under which the stock

was issued “provided not that the bondholders’ committee should receive the issue of stock from the plaintiff, but that the stock should be issued directly to and held only by the voting trustees” fully supports the judgment for the plaintiff and that the same should be affirmed.

Dated, San Francisco, California,
November 26, 1935.

Respectfully submitted,

LYMAN HENRY,
Attorney for Appellee.



United States
Circuit Court of Appeals
For the Ninth Circuit

R. J. RICHARDS,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Transcript of Record

Upon Petition to Review an Order of the United States
Board of Tax Appeals.

FILED

MAY 24 1935

PAUL P. O'BRIEN,

CLERK

United States
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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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Docket No. 52,848

R. J. RICHARDS,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

APPEARANCES.

C. E. McDOWELL, Esq.,

For Taxpayer.

JOHN H. PIGG, Esq.,

ELDEN McFARLAND, Esq.,

For Commissioner.

DOCKET ENTRIES.

1931

Feb. 14—Petition received and filed. Taxpayer notified. (Fee paid.)

Feb. 16—Copy of petition served on General Counsel.

Apr. 7—Answer filed by General Counsel.

Apr. 13—Copy of answer served on taxpayer. Circuit Calendar.

1933

Aug. 2—Hearing set for week of Sept. 11, 1933, at Long Beach, California.

Sept. 18—Hearing had before Mr. Marquette, Div. 1 on merits. Submitted on stipulation of facts. Stipulation of facts filed. Petitioner's brief due Oct. 18, 1933. Commissioner's brief due Nov. 4, 1933. Reply

1933

due Nov. 24, 1933. Board to serve copies.
Called Sept. 11.

Oct. 18—Brief filed by taxpayer 10/31/33 copy served.

Nov. 4—Brief filed by General Counsel.

Nov. 20—Reply brief filed by taxpayer. 11/21/33 copy served.

1934

Jan. 29—Opinion rendered, Mr. Marquette, Div. 1.
Judgment will be entered for the Commissioner.

July 12—Decision entered, Div. 1. Mr. Marquette.

Sept. 28—Stipulation for review by U. S. Circuit Court of Appeals for the Ninth Circuit filed.

Sept. 28—Petition for review by U. S. Circuit Court of Appeals (9) with assignments of error filed by taxpayer.

Sept. 28—Proof of service filed by taxpayer.

Oct. 31—Motion for extension of 30 days to prepare statement and transmit record filed by taxpayer.

Oct. 31—Order enlarging time to Dec. 28, 1934, to complete and transmit record entered.

Dec. 17—Statement of evidence lodged.

Dec. 17—Notice of lodgment of statement filed.

Dec. 17—Motion for extension of 30 days to prepare and transmit record filed by taxpayer.

Dec. 17—Order enlarging time to Jan. 28, 1935, to complete and transmit record entered.

1935

- Jan. 24—Motion for extension of 30 days to approve statement and transmit record filed by taxpayer.
- Jan. 24—Order enlarging time to Feb. 27, 1935, to complete and transmit record entered.
- Feb. 25—Motion for extension of 30 days from Feb. 28, 1935, to complete and transmit record filed by taxpayer.
- Feb. 25—Order enlarging time to March 30, 1935, to prepare evidence and transmit record entered. [1]*

1935

- Mar. 25—Praecipe with proof of service thereon filed by taxpayer.
- Mar. 25—Agreed statement of evidence approved and ordered filed.
- Mar. 29—Order enlarging time to April 30, 1935, for transmission and delivery of record entered. [2]

*Page numbering appearing at the foot of page of original certified Transcript of Record.

United States Board of Tax Appeals.

Docket No. 52,848

R. J. RICHARDS,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION.

The above named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (IT:AR:E-1. RCC-60D) dated December 18, 1930, and as a basis for his proceeding alleges as follows:

1. That your petitioner is an individual with his residence at 1211 West Avenue, Pasadena, California.

2. That notice of deficiency (a copy of which is attached and marked Exhibit "A") was mailed to the petitioner on December 18, 1930.

3. The taxes in controversy are income taxes for the calendar year 1927 and for \$486.69; and for the year 1928 and for \$12,552.81.

4. The determination of tax set forth in said notice of deficiency is based upon the following errors: [3]

(1) In the foregoing notice of deficiency is disclosed an over-assessment of \$3863.20 for the year 1926 and for which a claim for refund has

heretofore been filed by the petitioner. That petitioner consents to the allowance of such refund and makes no claim of error as to the determination by the Commissioner of Internal Revenue as to the correct tax liability of your petitioner for the year 1926.

(2) The erroneous holding by the Commissioner of Internal Revenue that the income received by petitioner for the calendar years 1927 and 1928 from three real estate trusts designated Nos. 2-1780, 2-1850 and 2-1899, in which trusts the Security-First National Bank of Los Angeles, Guaranty Office (as successor to the Security Trust & Savings Bank) is trustee, is not taxable under Sections 208 and 101 of the Revenue Acts of 1926 and 1928, respectively.

(3) The increase by the Commissioner of Internal Revenue under the foregoing erroneous conclusion of the tax liability of your petitioner for the year 1927 from the sum of \$19,644.87 to the sum of \$20,131.56, and for the year 1928 from the sum of \$14,600.30 to the sum of \$27,153.11.

(4) The determination by the Commissioner of Internal Revenue that the purpose for which an asset is being [4] held at the time of its sale is determinative of the taxable status of such asset, either as a capital asset or otherwise.

(5) The holding by the Commissioner of Internal Revenue that the fact that certain assets have once been established in the status of capital assets under said Sections 208 and 101, respectively, is

immaterial in determining the amount of tax to be paid by your petitioner.

(6) The holding that petitioner was engaged in any business in which the real estate constituting the corpus of said trusts was held primarily for sale.

(7) The holding by the Commissioner of Internal Revenue that the real estate constituting the corpus of said trusts, or any other real estate, was sold by petitioner during the years 1927 and 1928 in the course of any business.

(8) The holding by the Commissioner of Internal Revenue that the profits derived by the petitioner from the sale of real estate in said trusts above mentioned during the years 1926, 1927 and 1928 is not returnable as a capital net gain.

(9) The refusal by the Commissioner of Internal Revenue to permit petitioner to treat the net profits from the sale of lots in said trusts, at his option, either as ordinary net income or capital net gain. [5]

(10) The holding that the determination by the Commissioner of Internal Revenue for the year 1925 that the income from such trusts is taxable as capital net gain does not control the same issue for subsequent years.

5. The facts upon which petitioner relies as a basis of this proceeding are as follows:

a. That the petitioner now resides and has his principal place of business at 1211 West Avenue,

Pasadena, California. That prior thereto and during the year 1929 petitioner had his residence and office at 5162 Whittier Boulevard, Los Angeles, California. That prior to such time petitioner resided and had his office in Chicago, Illinois, and that all returns involved in this affidavit were joint returns made by petitioner for himself and wife.

b. That prior to the year 1920 and at all times since, the petitioner has been engaged in the business of raising, packing, buying and marketing lettuce, cauliflower and other farm products. That during all of such time petitioner has carried on said business under the firm name and style of W. M. Watson & Co., and since the year 1927 has carried on a similar business as a co-partner under the name of M. C. Wahl & Co. [6]

c. That petitioner has never engaged in the real estate business or in the business of buying, selling or subdividing real estate, nor has petitioner ever been a dealer in real estate, nor licensed as a salesman or broker under the laws of the State of California, or elsewhere, to buy or sell real estate, nor is petitioner a member of any real estate board or other organization of persons engaged in the purchase and sale of real estate, nor has petitioner any place of business from which he carries on or conducts any real estate business or the buying and selling of real estate, nor has petitioner ever made purchases or sales or dealt in any way with real estate for third persons.

d. That on or about the 15th day of September, 1920, Taxpayer acquired from Ysidora Coutts Fuller, by deed dated June 29, 1920, title to approximately forty-seven (47) acres of real estate in the County of Los Angeles, as is more particularly described in the deed by which title was conveyed to petitioner, a copy of which deed is attached to this petition and marked Exhibit "B". That said property referred to in said deed is for convenience hereinafter referred to as "Parcel 1".

e. That on or about the 30th day of April, 1921, petitioner acquired from one Pearl Holmgreen, by deed dated April 21, 1921, approximately four (4) acres immediately adjacent to and lying to the west of said Parcel 1, which [7] real property is more particularly described in the deed by which said petitioner acquired said title, a copy of which deed is attached hereto and marked Exhibit "C", and the parcel of land therein described is hereafter described as "Parcel 2".

f. That thereafter, on or about the 11th day of March, 1922, petitioner acquired title from the Winter Investment Company, by deed dated February 8, 1922, to certain real property adjacent to said Parcels 1 and 2, and lying to the south thereof, which said property is more particularly described in said deed, a copy of which is hereto attached and marked Exhibit "D". Said real property last mentioned is hereinafter referred to as "Parcel 3".

g. That said property, when purchased by petitioner, was purchased by him to use in raising lettuce and other farm products, and was held and used by petitioner for that purpose, and that said real property was not at any time purchased or held by petitioner primarily or at all for sale in the course of petitioner's trade or business, or otherwise.

h. That said real property was located not far from the City of Los Angeles, State of California, and after the purchase of said property the population of the City of Los Angeles increased very rapidly, and [8] other parcels of real estate located between said real property and the City of Los Angeles were subdivided, sold and populated, and increasing taxes, charges and assessments were levied against said real property, and said real property increased in value to such an extent that the further owning and operating of said property for the purpose of raising lettuce, cauliflower and other farm products, or any other use in the business of petitioner was unprofitable, and petitioner determined upon the sale of said property and the purchase of other property more suited for the transaction of petitioner's business.

i. That the business of petitioner required his absence from the City and County of Los Angeles during a considerable portion of each year, and as a matter of convenience for the sale of said real property, petitioner created from time to time three trusts designated as Nos. 2-1780, 2-1850 and 2-1899.

with the Guaranty Office of the Security Trust & Savings Bank, at Los Angeles, California. That said bank has since been succeeded by the Security-First National Bank of Los Angeles, a national banking association. That in the opinion of your petitioner, your petitioner was able to obtain a larger return from the sale of said property by subdi- [9] viding the same, rather than by selling the same in larger parcels, and for that reason your petitioner did subdivide said property and did employ one P. N. Snyder, a real estate agent and broker, to sell and dispose of the same.

j. That Trust No. 2-1780 was created by your petitioner on or about the 15th day of July, 1925, and to the said bank under the terms of said trust your petitioner conveyed a portion of Parcel 1. That thereafter sales were made of lots in said subdivision and the method of sale proving satisfactory to petitioner, petitioner, on or about August 6, 1926, created said Trust No. 2-1850 with said bank and conveyed thereto the remaining portion of said Parcel 1, all of Parcel 2 and a portion of Parcel 3. That thereafter lots were sold under said trust, and the method of sale proving satisfactory to your petitioner, petitioner did thereafter, on or about January 12, 1927, convey the remaining portion of said Parcel 3 to said bank in trust under said Trust No. 2-1899.

k. That audits had been made under the direction of the Commissioner of Internal Revenue of each and all of said three trusts, and said audits

have determined the amount of profit for the years 1926, 1927 and 1928, received by [10] the petitioner from each and all of said trusts, and your petitioner has accepted as correct the amount of profit only, as determined by said audit as the result of the sales of the property in each of said trusts.

l. That in the sale of lots in said three parcels above mentioned petitioner took no active part, but the promotion, advertising and sale of said lots was handled by the said P. N. Snyder in such a manner and to such an extent that the general public believed that the said P. N. Snyder was the owner of said property.

m. That said trusts were created by petitioner as a matter of convenience for the handling of sales contracts, collections and conveyances of the property above described, and that said trusts and the actions of the trustee thereon were subject to the order of the petitioner, and that said trusts have been varied from time to time as and when directed by the petitioner, and that the placing of said property in trust did not in any way limit the management, direction or control by the petitioner of the unsold portions of the property.

n. That the real property above described was all held by the petitioner for more than two (2) years prior to the sale of any portion thereof, and was not at any time during said period when the same was held by the petitioner [11] prior to the creation of said trusts held by the petitioner primarily or at all for sale during any of said period

of time, and that by reason thereof, at the time petitioner created each and all of said trusts the property placed by petitioner in each of said trusts had at the time it was so placed by petitioner become a "capital asset" and did thereafter retain and hold such character as a capital asset, and the sale of said property in lots or parcels, instead of as a whole, did not change the character of any portion of said real property from that of a "capital asset", nor did it make any taxable gain from the sale of said real property other than capital net gain.

o. That on or about December 17, 1828, the then acting Commissioner of Internal Revenue did enter into an agreement with the petitioner as to the final determination of taxability of your petitioner for the year 1925, and that in said agreement said acting Commissioner of Internal Revenue did recognize and determine that for the year 1925 the taxable income from the sale of said real property sold during said year 1925 was from the sale of "capital assets", and petitioner's tax liability for the year 1925 was thereupon computed accordingly, and that said determination hav- [12] ing been once made by the Commissioner of Internal Revenue, is thereafter binding upon the Treasury Department and the petitioner.

WHEREFORE, your petitioner prays that this Board may hear the proceedings and determine that the income received by your petitioner during the years 1927 and 1928 from the sale of said real estate in said Trusts No. 2-1780, 2-1850 and 2-1899 is tax-

able as a capital net gain and not as ordinary taxable income, and that the finding of the Commissioner of Internal Revenue that there is a deficiency chargeable against your petitioner for the year 1927 in the sum of \$486.69, and for the year 1928 in the sum of \$12,552.81 be vacated and found to be not in accordance with the Revenue Acts of 1926 and 1928.

C. E. McDOWELL,
Counsel for Petitioner
922 Security Title Ins. Bldg.,
Los Angeles, California.
[13]

STATE OF CALIFORNIA,
COUNTY OF LOS ANGELES.—ss.

R. J. RICHARDS, being duly sworn, says that he is the petitioner named in the foregoing petition; that he has read the foregoing petition and is familiar with the statements contained therein, and that the facts stated are true, except as to those facts stated to be upon information and belief, and those facts he believes to be true.

R. J. RICHARDS.

Subscribed and sworn to before me this 9th day of February, 1931.

[Notarial Seal]

MURIEL P. MONTGOMERY,
Notary Public in and for the County
of Los Angeles, State of California.

My Commission Expires Feb. 10, 1932. [14]

EXHIBIT "A"

Dec. 18, 1930

IT:AR:E-1

RCC-60D

Mr. R. J. Richards,

5162 Whittier Boulevard,

Los Angeles, California.

Sir:

You are advised that the determination of your tax liability for the years 1926, 1927 and 1928 discloses a deficiency of \$13,039.50 for the years 1927 and 1928 and an overassessment of \$3,863.20 for the year 1926, as shown in the statement attached.

In accordance with section 274 of the Revenue Act of 1926 and section 272 of the Revenue Act of 1928, notice is hereby given of the deficiency mentioned. Within sixty days (not counting Sunday as the sixtieth day) from the date of the mailing of this letter, you may petition the United States Board of Tax Appeals for a redetermination of your tax liability for the years in which a deficiency is disclosed.

HOWEVER, IF YOU DO NOT DESIRE TO PETITION, you are requested to execute the enclosed agreement form and forward it to the Commissioner of Internal Revenue, Washington, D. C., for the attention of IT:C:P-7. The signing of this agreement will expedite the closing of your returns by permitting an early assessment of any deficiency and preventing the accumulation of interest charges, since the interest period terminates thirty days after filing the enclosed agreement, or on the date assess-

ment is made, whichever is earlier; WHEREAS
IF NO AGREEMENT IS FILED, interest will
accumulate to the date of assessment of the defi-
ciency.

Respectfully,
DAVID BURNET,
Commissioner
By, (Signed) W. T. SHERWOOD,
Acting Deputy Commissioner.

Enclosures:
Statement
Form 882
Form 874

[15]

STATEMENT

IT:AR:E-1
RCC-60D

In Re: Mr. R. J. Richards,
5162 Whittier Boulevard,
Los Angeles, California.
Tax Liability

Year	Corrected	Tax		Deficiency
	Tax Liability	Previously Assessed	Overas- sessment	
1926	\$ 4,669.40	\$ 8,532.60	\$3,863.20	
1927	20,131.56	19,644.87		\$ 486.69
1928	27,153.11	14,600.30		12,552.81
Totals	\$51,954.07	\$42,777.77	\$3,863.20	\$13,039.50

Further reference is made to the reports of the
internal revenue agent in charge, Los Angeles, Cali-
fornia, covering an investigation of your income

tax liability for the years 1926, 1927 and 1928, to protests filed with the agent in charge and this office, also conferences held in the office of the agent in charge on January 11, 1930, and in this office on October 31, 1930, both with your representative, Mr. C. E. McDowell.

You are advised in connection with your contentions against the inclusion of income received from real estate trusts as ordinary income subject to both normal and surtax instead of treating amounts as capital net gain subject to tax at 12½%, that this office has consistently held that purpose for which an asset is being held at time of sale is determinative of the taxable status of the asset. The mere fact that a certain asset has once been established in the status of a capital asset within the meaning of sections 208 and 101 of the Revenue Acts of 1926 and 1928 respectively is immaterial. For the foregoing reasons this office is of the opinion that you were engaged in the business during the period involved and that the realty in question was held primarily for sale in the course of such business. Further, that the profit in dispute realized by you during the years involved is not taxable under the provisions of sections 208 and 101 of the Revenue Acts of 1926 and 1928, respectively.

Your contention that the closing agreement entered into for the year 1925 in which income from these trusts was taxed at capital net gain rates controls the issue for subsequent years is also denied for the reason that the closing agreement in question relates to the year 1925 only and has no

relation whatever to the treatment of income for any subsequent year. [16]

Mr. R. J. Richards

Statement.

This office holds that the income in question falls within the provisions of Section 704(b) of the Revenue Act of 1928 and General Counsel's Memorandum 6630, Cumulative Bulletin VIII-2, page 179. The adjustments as made by the examining officer are, therefore, sustained.

Your claim for refund for the year 1926 has been considered and allowed in its adjustment.

1926

Net income reported on return		\$68,260.79
Add:		
1 Reduction in loss from		
business	\$ 9,228.87	
2 Trust income	85,299.79	94,528.66
	<hr/>	<hr/>
Total		\$162,789.45
Deduct:		
3 Gain on sales		114,471.48
		<hr/>
Net income adjusted subject to surtax		\$ 48,317.97
Less:		
Dividends	\$ 463.97	
Interest on Liberty Bonds	1,310.44	
Personal exemption and		
credit for dependents	3,900.00	5,674.41
	<hr/>	<hr/>
Balance subject to normal tax		\$ 42,643.56

Normal tax at 1½% on \$4,000.00	\$ 60.00
Normal tax at 3% on \$4,000.00	120.00
Normal tax at 5% on \$34,643.56	1,732.18
Surtax on \$48,317.97	2,761.34
	<hr/>
Total	\$ 4,673.52
Less:	
Earned income credit	4.12
	<hr/>
Correct tax liability	\$ 4,669.40
Tax previously assessed	8,532.60
	<hr/>
Overassessment	\$ 3,863.20
	[17]

Mr. R. J. Richards

Statement

Explanation of Changes

1. This item represents reduction in depreciation, interest and taxes paid in the amounts of \$1,696.69, \$1,200.94 and \$7,421.43, respectively, less sales overstated in the amount of \$417.30 and amortization of the building erected on leased ground in the amount of \$472.89.

2. This item represents income received through trust transferred from line 6 of the return.

3. This item represents trust income eliminated from line 6.

1927

Net income reported on return		\$157,158.99
Add:		
1. Income from trust		144,953.58
		<hr/>
Total		\$302,112.57
Deduct:		
2. Business loss increased \$ 4,337.81		
3. Trust income	181,585.22	
4. Contributions	200.00	186,123.03
	<hr/>	<hr/>
Adjusted net income		\$115,989.54
Less:		
Dividends	\$ 1,836.03	
Interest on Liberty Bonds	298.07	
Personal exemption and credit for dependents	3,900.00	6,034.10
	<hr/>	<hr/>
Balance subject to normal tax		\$109,955.44
Normal tax at 11½% on \$4,000.00		\$ 60.00
Normal tax at 3% on \$4,000.00		120.00
Normal tax at 5% on \$101,955.44		5,097.77
Surtax on \$115,989.54		14,857.91
		<hr/>
Total		\$ 20,135.68

[18]

Mr. R. J. Richards	Statement.
Brought forward	\$ 20,135.68
Less:	
Earned income credit	4.12
	<hr/>
Correct tax liability	\$ 20,131.56
Tax previously assessed	19,644.87
	<hr/>
Deficiency	\$ 486.69

Explanation of Changes

1. This item represents corrected income received through trusts transferred from line 6 of the return.

2. This item represents increase in loss sustained through partnerships of Wahl and Company and Wahl and Richards.

3. This item represents an increase allowed in contributions.

1928

Net income reported on return	\$ 16,315.38
Add:	
Income from real estate trusts	129,908.62
	<hr/>
Adjusted net income	\$146,224.00
Less:	
Dividends	\$3,571.12
Interest on Liberty Bonds	350.00
Personal exemption and credit for dependents	3,900.00
	<hr/>
Balance subject to normal tax	\$138,402.88

Normal tax at 1½% on \$4,000.00	\$ 60.00
Normal tax at 3% on \$4,000.00	120.00
Normal tax at 5% on \$130,402.88	6,520.14
Surtax on \$146,224.00	20,904.80

Total tax	\$ 27,604.94
-----------	--------------

[19]

Mr. R. J. Richards

Statement.

Brought Forward

\$ 27,604.94

Less:

Earned income credit

451.83

Corrected tax liability

\$ 27,153.11

Tax previously assessed

14,600.30

Deficiency

\$12,552.81

The overassessment shown herein will be made the subject of a certificate of overassessment which will reach you in due course through the office of the collector of internal revenue for your district and will be applied by that official in accordance with section 284 of the Revenue Act of 1926.

A copy of this letter has been mailed to your representative, Mr. C. E. McDowell, 724 Pacific Finance Building, Los Angeles, California, who has on file in this office a duly recorded power of attorney.

GB-2

[20]

EXHIBIT "B"

GRANT DEED

I, YSIDORA COUTS FULLER, a widow, in consideration of TEN and 00/100 Dollars, to me in hand paid, the receipt of which is hereby acknowledged, do hereby GRANT to ROBERT JAMES RICHARDS and ARABELLA GRACE RICHARDS, husband and wife, as Joint Tenants, with the right of survivorship, all that real property situate in the County of Los Angeles, State of California, described as follows:

All that certain portion of the Rancho Laguna, so-called, in the Rancho San Antonio, County of Los Angeles, State of California, described as follows:

Beginning at an iron pipe, set in the Southerly line of the Whittier Road, at the most Easterly corner of Lot Twenty-one (21), Rancho Laguna, and running thence along the Easterly line of said Lot Twenty-one (21), South twenty-six degrees (26°) eighteen minutes ($18'$) twenty seconds ($20''$) West, thirteen hundred eight and twenty-two hundredths (1308.22) feet to an iron pipe set at the most Southerly corner of said Lot Twenty-one (21); thence along the Southerly line of said Lot Twenty-one (21) and Lot Twenty (20), North seventy-five degrees (75°) thirty-seven minutes ($37'$) West thirteen hundred thirty-one and fifty-seven hundredths (1331.57) feet to an iron pipe set at a point six hundred sixty-four and forty-nine hundredths (664.49) feet, North seventy-five (75°)

thirty-seven minutes (37') West from the most Westerly corner of said Lot Twenty-one (21); thence North fourteen degrees (14°) twenty-three minutes (23') East twelve hundred eighty (1280) feet to an iron pipe set in the Southerly line of the Whittier Road, at a point six hundred sixty-four and forty-nine hundredths (664.49) feet North seventy-five degrees (75°) thirty-seven minutes (37') West from the most Northerly corner of said Lot Twenty-one (21); thence along the Southerly line of said Whittier Road, South seventy-five degrees (75°) thirty-seven minutes (37') East sixteen hundred one and eighty-two hundredths (1601.82) feet to the point of beginning.

The same comprising the Easterly part of Lot Twenty (20), and all of Lot Twenty-one (21) as delineated on a map entitled Map of the Rancho Laguna and thereon marked with the name of "Ysidora Coutts Fuller", said map being the map filed as Exhibit "A" in connection with the Referee's Report in Action No. B-25296 of the Superior Court in Los Angeles County, entitled Ysidora Coutts Fuller vs. Cave J. Coutts et al.

SUBJECT TO: Taxes for the fiscal year 1920-21 TO HAVE AND TO HOLD to the said grantees, as Joint Tenants, with [21] the right of survivorship.

WITNESS my hand this 29th day of June, 1920.

YSIDORA COUTS FULLER.

STATE OF CALIFORNIA,
COUNTY OF LOS ANGELES.—ss.

On this Eleventh day of September, 1920, before me, W. F. Cook, a Notary Public in and for said County, personally appeared YSIDORA COUTS FULLER, a widow known to me to be the person whose name is subscribed to the foregoing instrument and acknowledged that she executed the same.

WITNESS my hand and Official Seal.

[Notarial Seal] W. F. COOK,
Notary Public in and for the County
of Los Angeles, State of California.

COMPARED

DOCUMENT— LUFKIN
BOOK— EASTON

RECORDED AT REQUEST OF LOS ANGELES
TITLE INS. CO. Sep. 15 1920 at 8:30 A.M. in
Book 7306, Page 332 of Deeds Records, Los Angeles
County, Cal.

C. L. LOGAN, County Recorder.

I certify that I have correctly transcribed this document in above mentioned book.

C. HUNTER,
Copyist, County Recorder's Office,
L. A. Co., Cal. [22]

EXHIBIT 'C'.

GRANT DEED.

I, Pearl Holmgreen, a single woman: in consideration of TEN DOLLARS to me in hand paid, the

receipt of which is hereby acknowledged, do hereby GRANT TO Robert James Richards and Arabella Grace Richards, husband and wife, as joint tenants; all that real property situate in the County of Los Angeles, State of California, described as follows:

Beginning at an iron pipe set in the Southerly line of the Whittier Road, at a point 664.49 feet North $75^{\circ} 37'$ West from the most northerly corner of Lot 21, Rancho Laguna, and running thence South $14^{\circ} 23'$ West 1280 feet to an iron pipe set in the southerly line of Lot 20, Rancho Laguna, at a point 664.49 feet from the most Westerly corner of said Lot 21; thence along the Southerly line of said Lot 20 North $75^{\circ} 37'$ West 138.06 feet to an iron pipe; thence North $14^{\circ} 23'$ East 1280 feet to an iron pipe set in the Southerly line of the Whittier Road; thence along the Southerly line of Whittier Road, South $75^{\circ} 37'$ East 138.06 feet to the point of beginning,—the same comprising a portion of Lot 20, as delineated on said Map, Exhibit "A", attached to the Final Decree in Partition in Action No. B-25296 of the Superior Court of Los Angeles County, a certified copy of which Decree is recorded in Book 6387 of Deeds, page 1, Records of Los Angeles County, California, containing 4,057 acres.

SUBJECT TO taxes for the fiscal year 1921-1922; TO HAVE AND TO HOLD to the said grantees in joint tenancy WITNESS my hand this 21st day of April, 1921.

PEARL HOLMGREEN. [23]

STATE OF CALIFORNIA,
COUNTY OF LOS ANGELES.—ss.

On this 21st day of April, 1921, before me, F. H. Greene, a Notary Public in and for said County, personally appeared Pearl Holingreen, a single woman; known to me to be the person whose name is subscribed to the foregoing instrument, and acknowledged that she executed the same.

WITNESS my hand and Official Seal.

[Notarial Seal]

F. H. GREENE,

Notary Public in and for the County of Los Angeles, State of California.

COMPARED.

Document.....

Van Velsir

Book.....

Tower

RECORDED AT REQUEST OF TITLE INSURANCE & TR. CO. Apr 30 1921 at 8:30 A. M. in Book 185 Page 307 of Official Records, Los Angeles County, Cal.

C. L. LOGAN, County Recorder.

I certify that I have correctly transcribed this document in above mentioned book.

M. CHICK,

Copyist, County Recorder's Office, L. A. Co., Cal.

[24]

EXHIBIT "D"

GRANT DEED.

(Code) Corporation.

WINTER INVESTMENT COMPANY,

of the City and County of Los Angeles, State of California, a Corporation duly organized and existing under and by virtue of the laws of the State of California, and having its principal place of business in the City of Los Angeles, County of Los Angeles, and State of California, FOR AND IN CONSIDERATION OF THE SUM OF Ten and NO/100 Dollars, the receipt whereof is hereby acknowledged, does hereby GRANT TO ROBERT JAMES RICHARDS and ARABELLA GRACE RICHARDS, his wife, as joint tenants with right of survivorship:

ALL THAT REAL PROPERTY, described as follows, to-wit: All that certain portion of the Rancho Laguna, so called, in the Rancho San Antonio, County of Los Angeles, State of California, described as follows: Beginning at an iron pipe set in the Northerly line of Lot Twenty-three (23), Rancho Laguna, at a point four hundred ninety-eight and eighty-five hundredths (498.85) feet North seventy-five degrees (75°) thirty-seven minutes (37') West from the most Easterly corner of said Lot Twenty-three (23), and running thence South fourteen degrees (14°) twenty-three minutes (23') West twenty hundred forty-four and sixty-nine hundredths (2044.69) feet to an iron pipe set in the

North Easterly line of Anaheim Telegraph Road at a point eight hundred forty-seven and thirty hundredths (847.30) feet South sixty-one degrees (61°) twenty minutes (20') forty-five seconds (45'') East from the most Westerly corner of said Lot Twenty-three (23); thence along the North Easterly line of the Anaheim Telegraph Road North sixty-one degrees (61°) twenty minutes (20') forty-five seconds (45'') West eight hundred forty-seven and thirty hundredths (847.30) feet to an iron pipe at the most Westerly corner of said Lot Twenty-three (23); thence North fourteen degrees (14°) twenty-three minutes (23') East along the Westerly line of said Lot Twenty-three (23) eighteen hundred thirty-five and eighty-three hundredths (1835.83) feet to an iron pipe set in the Northerly corner of said Lot Twenty- [25] three (23); thence along the dividing line between Lots Twenty (20) and Twenty-three (23) South seventy-five degrees (75°) thirty-seven minutes (37') East eight hundred twenty-one and fifteen hundredths (821.15) feet to the point of beginning. The same comprising the Westerly portion of Lot Twenty-three (23), as delineated on a map entitled "Map of the Rancho Laguna" and thereon marked with the name of "John F. Coutts", said map being the map filed as Exhibit "A" in connection with the Referee's Report in Action No. B-25296 of the Superior Court in Los Angeles County, entitled Ysidora Coutts Fuller vs. Cave J. Coutts, et al, and attached to Final Decree of Partition of said Action, a

certified copy of which decree is recorded in Book 6387 Page 1 et seq., of Deeds in the office of the County Recorder of said County.

IN WITNESS WHEREOF, the said party of the first part has caused its corporate name and seal to be affixed by its President and Secretary thereunto duly authorized this 8th day of February, nineteen hundred and twenty-two.

[Corporate Seal]

WINTER INVESTMENT COMPANY,
BY GEORGE F. WINTER,

President,

BY FRANK C. WINTER,

Secretary.

STATE OF CALIFORNIA,
COUNTY OF LOS ANGELES.—ss.

ON THIS 10th day of February A. D., 1922, before me, Margaret F. Brennan, a Notary Public in and for the said County and State, residing therein, duly commissioned and sworn, personally appeared George F. Winter known to me to be the President and Frank C. Winter known to me to be the Secretary of the Winter Investment Company, the corporation that executed the within Instrument, known to me to be the persons who executed the within Instrument, on behalf of the Corporation therein named, and acknowledged to me that such Corporation executed the same.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my official seal the day and year in this certificate first above written.

[Notarial Seal] MARGARET F. BRENNAN,
Notary Public in and for said County and State.
[26]

COMPARED.

DOCUMENT.....
BOOK.....

WICKS
McEWEN

RECORDED AT REQUEST OF TITLE INSURANCE & TR. CO. Mar 11 1922 at 8:30 A. M.
In Book 963 Page 92 of Official Records, Los Angeles County, Cal.

C. L. LOGAN, County Recorder.

I certify that I have correctly transcribed this document in above mentioned book.

C. FLETCHER,

Copyist, County Recorder's Office, L. A. Co., Cal.
[Endorsed]: Filed February 14, 1931. [27]

[Title of Court and Cause.]

ANSWER.

The Commissioner of Internal Revenue, by his attorney, C. M. Charest, General Counsel, Bureau of Internal Revenue, for answer to the petition of the above-named taxpayer, admits and denies as follows:

1. Admits that the petitioner is an individual and denies any knowledge or information sufficient to form a belief as to the truth of the remaining allegations contained in Paragraph 1 and therefore denies the same.

2. Admits the allegations contained in Paragraph 2.

3. Admits the allegations contained in Paragraph 3.

4. (1) Answering Subparagraph (1) of Paragraph 4 of the petition, the respondent says that the Board has no jurisdiction of the tax liability of the petitioner for the year 1926, with respect to which the respondent has determined an over-assessment as set forth in deficiency notice, a copy of which is attached to the petition as Exhibit A.

(2) (3) (4) (5) (6) (7) (8) (9) (10). Denies that he erred in determining the tax set forth in said notice of deficiency and further denies that he erred as alleged in Paragraphs 4(1) to 4(10) of the petition.

5. Denies each and every material allegation contained in Paragraphs 5(a) to 5(o) of the petition which is inconsistent with or contrary to the determination of the respondent as set forth in the statement accompanying the notice of deficiency, which is attached to and made a part of the petition, as Exhibit A.

6. Denies generally and specifically each and every material allegation [28] contained in tax-

payer's petition not hereinbefore admitted, qualified or denied.

WHEREFORE, it is prayed that the taxpayer's appeal be denied.

(Signed) C. M. CHAREST,
General Counsel,
Bureau of Internal Revenue.

JOHN H. PIGG,
Special Attorney,
Bureau of Internal Revenue,
Of Counsel.

k 4-4-31

[Endorsed]: Filed April 7, 1931. [29]

United States Board of Tax Appeals.

Docket No. 52848. Promulgated June 29, 1934.

R. J. RICHARDS,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

A taxpayer who owned land which had been devoted to farming purposes and which became too valuable for those purposes, through agents employed by him, subdivided and improved it, and after advertisement sold the lots. This course continued through at least three years. Held, that the

lots were held by the taxpayer primarily for sale in the course of his business and that he is not entitled to the benefits of sections 208 of the Revenue Act of 1926 and 101 of the Revenue Act of 1928.

C. E. McDowell, Esq., for the petitioner.

Elden McFarland, Esq., for the respondent.

OPINION.

MARQUETTE: The respondent has determined deficiencies in income tax for the years 1927 and 1928 in the respective amounts of \$486.69 and \$12,552.81. The only issue is whether certain real estate sold in the taxable years constituted capital assets within the meaning of section 208 (a) (8) of the Revenue Act of 1926, and section 101 (c) (8) of the Revenue Act of 1928.

This proceeding was submitted upon a stipulation of the parties to the effect that two affidavits of the petitioner, one dated October 20, 1930, together with exhibits thereto attached, and the other dated September 15, 1933, might be received in evidence, and that the respondent agreed that if the petitioner was called as a witness he would testify as set forth in the affidavit. However, respondent did not agree that all of the facts and conclusions stated in the affidavits were correct. The affidavits and exhibits are made a part of this report.

The material facts are that the petitioner and his wife made joint income tax returns for the years before us, and that the real property involved was

acquired by them as joint tenants with the right of survivorship. Since prior to 1920 the petitioner, for himself or [30] as a member of a partnership, has been engaged in the business of raising, packing, buying, and marketing farm products, particularly lettuce. About September 15, 1920, petitioner and his wife acquired title to approximately 47 acres of land in Los Angeles County, California. About April 30, 1921, they acquired another tract adjoining the above tract, containing about 4 acres. About March 11, 1922, they acquired title to a third piece of land adjacent to the foregoing tracts. These tracts of land at the time of acquisition lay in a very productive farming area and were used by the petitioner in the raising of lettuce and sometimes chicory and endive. They were surrounded by farm lands producing these same vegetables. The products of these adjacent lands, together with the products of the petitioner's own lands, enabled him to make shipments in car-load lots.

In 1921 the petitioner erected buildings and other structures on not over three and one half acres of these lands, which were thereafter used by him as a combined office and residence.

After the petitioner acquired these properties there was a great deal of real estate activity in the lands between his property and the boundary of the city of Los Angeles. The intervening property began to be subdivided and sold, with the result that the petitioner's property rapidly increased in

value until it arrived at a value in excess of \$4,000 an acre without improvements. Taxes and assessments for local improvements also increased. The taxes on this property in 1920 were \$657.84 and for 1924 were \$5,903.22, in addition to which the petitioner was required to pay \$4,479.95 in 1924 on account of special assessments. This rise in prices made the use of these lands and the adjacent lands for gardening purposes unprofitable, and in this way deprived the petitioner of a base from which to ship the vegetables in carload lots.

In 1925 petitioner determined to subdivide a part of the first parcel of land which he had purchased. In pursuance of this plan on July 15, 1925, he conveyed a portion of the property to the Security Trust & Savings Bank of Los Angeles (now Security Trust National Bank of Los Angeles) hereinafter referred to as the bank, which accepted it in trust to secure a note of \$28,500 which petitioner and his wife owed the bank, and upon further trust to subdivide and sell the property conveyed. Under the deed of trust petitioner and his wife agreed to pay all taxes and assessments levied on the property, to pay principal and interest on all indebtedness secured by the trust, to pay all claims, liens and encumbrances and defend all suits affecting the property, to pay for all improvements ordered by him or his agent, and to file with the trustee a copy of each contract for improvements to be placed on the property. [31] The property was to be subdivided and improved by the petitioner and his wife.

The deed contained provisions which permitted the trustee, upon default of petitioner and his wife in paying the above amounts, to pay them itself, and gave it recourse against the property. The trustee was authorized to rent, sell and convey the property or any part thereof to such persons and at such times as it deemed best, provided the sale prices of the lands should not be less than those indicated in the schedule to be filed with the deed. The proceeds received from the sales were to be used to pay commissions and to release liens, the balance to go in what was termed a general fund, out of which the cost and expenses of the trust and certain other expenses were to be paid, and what remained over was to be paid to the petitioner and his wife. The deed recites that at the request of the petitioner and his wife it appointed P. N. Snyder "as their exclusive agent to subdivide and improve, and to solicit and obtain purchasers for such part of said property" as was subdivided. He was paid a commission, out of which he was to pay for advertising and other selling expenses of himself and his subagents. Among the duties assumed by the agent was the general care and custody of the subdivided property, and of all improvements placed upon the property, which included the installation of gas, water and electricity. The trustee was not required to procure any insurance on any building upon the property, or to collect or disburse any rentals therefrom. These duties were to be performed by the petitioner and his wife.

Upon payment in full of the indebtedness secured by the deed and at the request in writing of petitioner and his wife, the trustee was given authority to close and terminate the trust, but was not required to do so as long as any of the covenants contained in any deed remained unperformed. The petitioner and his wife furnished the trustee a list of the minimum prices at which the lots were to be sold. The number of lots was 186. The minimum price was \$1,250 and the maximum price was \$40,000 per lot.

The sales of lots in the first subdivision having proved satisfactory, petitioner determined to subdivide other portions of the property above described. By deed of August 6, 1926, the bank accepted in trust property previously conveyed. The provisions of this trust deed resembled the one of July 15, 1925. Afterward, the petitioner and his wife determined to subdivide and sell the remaining portion of the property purchased as hereinabove set forth, and by deed of trust dated January 12, 1927, the bank accepted such property on practically the same trusts as those provided in the deed of July 15, 1925. [32]

The principal reason for the above conveyances was to have all deeds on lots promptly executed, especially in the absence of the petitioner from Los Angeles. The number of lots in the second subdivision above set forth was 82. The number of lots in the third subdivision was 152. In the third subdivision the minimum price for the lots was

\$1,200 and the maximum was \$15,000. Under each of the deeds, Snyder was appointed by the bank as petitioner's exclusive agent, at their request, for a term of eight months, with the right to serve eight months more upon achieving certain results, and upon the termination of his employment the trustee was to appoint as agent for the petitioner and his wife such person as they directed, all sales, however, to be subject to the approval of the trustee of the bank. The petitioner's business of producing, packing and selling lettuce and other vegetables increased from year to year, and he substituted, either by lease or purchase, farming properties for the properties which he subdivided. The petitioner, himself, has never taken part in the subdivision or the sale of the lots in the subdivisions, all of which was done by Snyder. Except as herein set forth, the petitioner has never engaged in the business of buying and selling real estate or dealt therein. He has not been licensed as a broker to buy or sell real estate.

The petitioner seeks to have the gain derived from the sale of the lots in his subdivisions taxed under the provisions of section 208 of the Revenue Act of 1926 and section 101 of the Revenue Act of 1928. The only issue is whether the lands from which the lots were carved constituted "capital assets" as that term is defined in the above sections. Section 208 (a) (8) of the Revenue Act of 1926 provides:

The term "capital assets" means property held by the taxpayer for more than two years (whether

or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale in the course of his trade or business. * * *

Section 101 (c) (8) of the Revenue Act of 1928 is not materially different. If we eliminate the intervention of the trustee, it is clear that petitioner and his wife at the dates of the various sales had held the lands for more than two years. We do not think the fact that when the sales were made the legal title was in the trustee, is material. The conveyances were made for two purposes—first, to secure the bank, which was also trustee, for its loan then made to petitioner and his wife and to secure it for the advances thereafter to be made, and, second, to facilitate the execution and delivery of deeds to purchasers of the lots in the absence of the petitioner. On them, as individuals, remained the duty of paying all taxes and liens [33] and advancing the money with which to pay the cost of subdivision and improvements and of insurance on the improvements. After paying the debts secured by the deeds and the cost and expenses of the trust and of the sales, what was left, corpus and income, was to be paid to the petitioner and his wife. The petitioner and his wife possessed all the substantial rights of ownership. The lands were held by them within the meaning of the above provisions. Car-

rie E. Molter, 19 B.T.A. 911; *affd.*, 60 Fed. (2d) 498; San Martinez Oil Co., 25 B.T.A. 218.

Real estate may not be included in inventory. Willard Pope, 28 B.T.A. 1255, and cases cited. The facts show, and counsel for the petitioner concedes, that the lots were held primarily for sale. There remains for solution the question whether they were so held by the petitioner "in the course of his * * * business".

The fact that the petitioner was in the business of producing and marketing vegetables did not preclude him from engaging in another distinct business. Counsel for the petitioner concedes this and such is the law. Ignaz Schwinn, 9 B.T.A. 1304; John D. Roney, 26 B.T.A. 1213, *affd.*, 67 Fed. (2d) 165. Neither do we think it is material that these lands, which were the individual properties of the petitioner and his wife, were once used by them in the farming business. Such use was abandoned and the lands were devoted to a very different purpose. There is nothing in the sections involved which makes any reference to the purpose for which the assets were acquired. To illustrate, one may, as here, own land devoted to farming and, having discovered minerals below the surface, proceed to mine and dispose of the minerals. The fact that he once used the land in connection with farming does not detract from the fact that he thereafter used it in the business of mining.

We may here dispose of the issue raised by the petitioner that in disposing of the lots by sale he

was liquidating his business of farming, or at least a part of it. He relies on Trustees for the Creditors and Stockholders of Gonzolus Creek Oil Co. (dissolved), 12 B.T.A. 310; Wilson Syndicate Trust, 14 B.T.A. 508; Dauphin Deposit Trust Co., Trustee, 21 B.T.A. 1214; G. F. Sloan, 24 B.T.A. 61; Blair v. Wilson Syndicate Trust, 36 Fed. (2d) 43; White v. Hornblower, 27 Fed. (2d) 277. We do not perceive the relevancy of these cases. Not only has the petitioner not liquidated his business of farming, but, as we read the record, he has enlarged it. What he has done is to take certain assets individually owned and devoted them to a new purpose.

Cleared of all obscurities, the issue is whether in doing this the petitioner engaged in a business. In attempting to define this term we said, in Willard Pope, *supra*: [34]

In Flint v. Stone Tracy Co., 220 U.S. 107, the Court said:

“Business” is a very comprehensive term and embraces everything about which a person can be employed. Black’s Law Dict. 158, citing *People ex rel. Hoyt v. Tax Comrs.*, 23 N.Y. 242, 244. “That which occupies the time, attention, and labor of men for the purpose of a livelihood or profit.” 1 Bouvier’s Law Dict. p. 273.

On the other hand, isolated transactions do not constitute the carrying on of a trade or business. *Mente v. Eisner*, 266 Fed. 161; *Bedell v. Commissioner*, 30 Fed. (2d) 622; *Washburn v. Commis-*

sioner, 51 Fed. (2d) 949. It is often difficult to apply the general definitions, with the result that "the decision in each instance must depend upon the particular facts before the court". *Von Baumbach v. Sargent Land Co.*, 242 U.S. 503.

Here we have no isolated transactions. Two of the subdivisions were laid out in 1925 and one in January 1927. The total number of lots in the three subdivisions was 420. Streets and alleys were laid out and, we assume, were improved. The trust deeds disclose elaborate provisions for improvements and places the cost of them on the petitioner and his wife. What these improvements were is not disclosed, except that they included the installation of gas, water and electricity. We are informed that rentals were to be collected by the petitioner and his wife, and that all insurance was to be procured and paid for by them. All this involved the expenditure of money and that money was to be raised and paid by these same individuals. If these provisions were not carried out, the burden rested on the petitioner to so show. This he has failed to do, and he must bear the consequences. A selling agent was employed and he was to have subagents. He was to have charge of advertising. Here we have continuity of effort. All this was done for gain, and it falls squarely within the concept of the term "business". Whose business was it? The plan was conceived by the petitioner who, with his wife, owned all the assets of the business. The fact that to a large extent he confided the management

of this business to his agent, Snyder, and to the trustee, does not make it any the less his business. As we said in Willard Pope, *supra*, “it is axiomatic that one may confide the management of his business to another; but it still remains the business of the owner”.

We are of opinion that the lots were held by the petitioner primarily for sale in the course of his business. Willard Pope, *supra*. Cf. *Sloan v. Commissioner*, 63 Fed. (2d) 666; affirming 24 B.T.A. 61.

Judgment will be entered for the respondent. [35]

United States Board of Tax Appeals

Washington

Docket No. 52,848

R. J. RICHARDS,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION.

Pursuant to the determination of the Board, as set forth in its report promulgated June 29, 1934, it is

ORDERED and DECIDED: That there are deficiencies of \$486.69 and \$12,552.81 for the years 1927 and 1928, respectively.

[Entered]: July 12, 1934.

[Seal] (s) JOHN J. MARQUETTE,

Member. [36]

In the United States Circuit Court of Appeals
of the Ninth Circuit.

B. T. A. No. 52,848

R. J. RICHARDS,

Petitioner on Review,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent on Review.

STIPULATION DESIGNATING CIRCUIT
COURT OF APPEALS.

IT IS HEREBY STIPULATED IN WRITING by and between the petitioner and respondent herein that the United States Circuit Court of Appeals for the Ninth Circuit shall be and the same is hereby designated as the Circuit Court of Appeals by which the decision of the Board of Tax Appeals herein may be reviewed, as provided in section 1002 of the Revenue Act of 1926 as amended.

Dated, September 28, 1934.

C. E. McDOWELL,

Attorney for Petitioner.

FRANK J. WIDEMAN,

Attorney for Respondent.

[Endorsed]: Filed Sep. 28, 1934. [37]

In the United States Circuit Court of Appeals
of the Ninth Circuit.

B. T. A. No. 52,848

R. J. RICHARDS,

Petitioner on Review,
vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent on Review.

PETITION FOR REVIEW OF DECISION OF
THE BOARD OF TAX APPEALS.

To the Circuit Court of Appeals for the Ninth
Circuit:

Your petitioner R. J. Richards, respectfully
shows:

First. This is a proceeding for review by the United States Circuit Court of Appeals for the Ninth Circuit of a decision of the United States Board of Tax Appeals in which the findings of fact and opinion of the Board of Tax Appeals were promulgated and entered on June 29, 1934, and the decision or "Final Order of Redetermination", entered on July 12, 1934, and which redetermined a deficiency in income tax against petitioner in the sum of \$486.69, for the year 1927, and in the sum of \$12,552.81, as to the year 1928.

Second. That your petitioner was on June 29, 1934, and has been at all times since and now is a resident and inhabitant of the City of Pasadena, County of Los Angeles, State of California, and

that the return of the taxes in [38] respect to which the alleged liability arises was made by your petitioner to the office of the Collector of Internal Revenue at the City of Chicago, County of Cook, State of Illinois. That the Commissioner of Internal Revenue and your petitioner have by a stipulation in writing designated United States Circuit Court of Appeals for the Ninth Circuit as the Court by which such decision of said Board of Tax Appeals may be reviewed.

Third. The nature of the controversy before the Board of Tax Appeals was the redetermination of income taxes under the Revenue Acts of 1926 and 1928, respectively, involving a determination of:

1. Whether or not, during the years 1927 and 1928, lots in tracts numbered 8790, 9436 and 9797, all in Los Angeles County, California, and held in trust, constituted "capital assets" of the petitioner within the meaning of section 208 (a) of the Revenue Act of 1926, and section 101 (c) of the Revenue Act of 1928.

2. Whether or not the income received by petitioner through the sale of said lots in such tracts, during the years 1927 and 1928, may be treated by petitioner as "capital net gain" under said sections and subject to a tax of $12\frac{1}{2}\%$, instead of the statutory normal and surtaxes.

Fourth. The errors committed by the Board of Tax Appeals on which your petitioner relies as the basis for this proceeding are as follows:

1. The Board erred in its conclusion that your petitioner was engaged, during the years involved, in [39] any other business than the business of producing and marketing vegetables and other farm products.

2. The Board erred in its conclusion that the real property constituting the tracts above mentioned, required by the petitioner and his wife in such business of producing and marketing farm products was ever devoted to a purpose not connected with such business.

3. The Board erred in its conclusion that the sale, through said trusts, by your petitioner of said real property was not a partial liquidation of petitioner's said business in so far as said business required the use or ownership of said lots.

4. The Board erred in its conclusion that the issue raised by petitioner was whether petitioner in selling lots in said tracts, during the years 1927 and 1928, through said trusts, was engaged in a business.

5. The Board erred in its conclusion that the lots in said tracts, sold through said trusts, were held by the petitioner primarily for sale in the course of his business.

6. That the Board erred in its conclusion that petitioner is not entitled to the benefits of section 208 of the Revenue Act of 1926, and section 101 of the Revenue Act of 1928, in computing and determining the income taxes of your petitioner during the years 1927 and 1928, with reference to the profits

made by your petitioner from the sale of lots [40] in the tracts above mentioned, through such trusts.

7. That the Board erred in redetermining a deficiency in income taxes against your petitioner in the sum of \$486.69 for the year 1927, and in the sum of \$12,552.81 for the year 1928.

WHEREFORE, your petitioner prays that this court may review the action of the Board of Tax Appeals in this cause, reverse the decision of the Court and direct the entry of a decision by said Board determining that there is no deficiency in income tax, for the years 1927 and 1928, due from your petitioner, and for such other and further relief as to the Court may seem meet and proper in the premises.

C. E. McDOWELL,
Attorney for Petitioner,
810 Title Guarantee Bldg.
Los Angeles, Calif.

[Endorsed]: Filed Sep. 28, 1934. [41]

STATE OF CALIFORNIA,
COUNTY OF LOS ANGELES.—ss.

C. E. McDOWELL, being duly sworn, says:

I am the attorney for the petitioner in this proceeding. I prepared the foregoing petition and am familiar with the contents thereof. The allegations of fact contained therein are true to the best of my knowledge, information and belief. This petition is not filed for purposes of delay, and I believe the petitioner is justly entitled to the relief sought.

C. E. McDOWELL.

Subscribed and sworn to before me this 22nd day of September, 1934.

[Notarial Seal] DOROTHY A. LEVOY,
Notary Public in and for the County of Los
Angeles, State of California. [42]

[Title of Court and Cause.]

NOTICE.

TO ROBERT H. JACKSON, ESQ.,
Assistant General Counsel for Internal Revenue,
Washington, D. C.

Please take notice that the above named petitioner has this day filed with the Clerk of the United States Board of Tax Appeals petition for review of the Board's decision rendered herein by the United States Circuit Court of Appeals for the Ninth Circuit. A copy of said petition for review and assignments of error are attached hereto as a part of this notice.

Dated this the 24th day of September, 1934.

(Signed) C. E. McDOWELL,
Attorney for Petitioner.

Service of foregoing notice and receipt of copy of petition for review is acknowledged this the 28th day of September, 1934.

ROBERT H. JACKSON,
Assistant General Counsel for Internal Revenue
Attorney for Respondent.

[Endorsed]: Filed Sep. 28, 1934. [43]

United States Board of Tax Appeals.

Docket No. 52,848

R. J. RICHARDS,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

STATEMENT OF EVIDENCE.

At the hearing of the above entitled proceeding, held before the United States Board of Tax Appeals on the day of September, 1933, the following stipulation between the parties in reference to the testimony of witnesses and documents offered in evidence was received and considered by the Board as all the material evidence pertinent to the issues in controversy, viz.:

STIPULATION.

It is stipulated by and between the above-named parties by their respective counsel, that the affidavit of R. J. Richards, dated October 20, 1930, together with the exhibits attached thereto, and the affidavit of R. J. Richards dated September 15, 1933, both of which are attached hereto, [44] may be received in evidence as the petitioner's case. Respondent agrees that R. J. Richards, if called as a witness, would testify as set forth in these affidavits. Respondent does not stipulate that all of the facts or conclusions stated are correct.

It is further stipulated that the matter may be submitted upon the presentation of this stipulation, together with the attached exhibits.

The affidavit of R. J. Richards dated October 20, 1930, together with the exhibits attached thereto, is in the words and figures as follows:

STATE OF CALIFORNIA,
COUNTY OF LOS ANGELES—ss.

ROBERT JAMES RICHARDS,
being first duly sworn, deposes and says:
The Taxpayer.

That his name is Robert James Richards, and that he now resides and has his principal place of business at 1211 West Avenue, Pasadena, California. That prior to taking up his residence at such address, and during the year 1929, the Taxpayer had [45] his residence and office at 5162 Whittier Boulevard, Los Angeles, California. That prior to such time Taxpayer resided and had his office in Chicago, Illinois. That all returns involved in this affidavit are joint returns made by Taxpayer for himself and wife. That the real property hereinafter referred to was acquired by the Taxpayer and his wife, as joint tenants with the right of survivorship, and all transactions with reference to same were carried on in joint names, but because Taxpayer at all times, either with written or oral consent of his wife, carried on any business transactions with reference to same, Taxpayer is, for the purposes of this affidavit, considered the owner of said real property.

Character of Business.

That prior to the year 1920 and at all times since, the Taxpayer has been doing business under the firm name and style of W. M. Watson & Co., and engaged in raising, packing, buying and marketing farm products, and particularly, lettuce. That the transaction of such business required the Taxpayer to travel and be away from his place of residence on numerous occasions.

That during and since the year 1927 Taxpayer [46] has been carrying on a similar business as a co-partner under the name of M. C. Wahl & Co. in Imperial County, California.

That affiant has never engaged in the real estate business or in the business of buying and selling real estate, nor has Taxpayer ever been a dealer in real estate, nor licensed as a broker or salesman under the laws of the State of California, or elsewhere, to buy and/or sell real estate, nor is affiant a member of any real estate board or other organization of persons engaged in the sale of real estate, nor has Taxpayer any place of business from which he carries on or conducts any real estate business or the buying and selling of real estate, nor has affiant ever made purchases or sales or dealt in any way with real estate for third persons.

Real Estate Involved.

That on or about the 15th day of September, 1920, Taxpayer acquired from Ysidora Coutts Fuller, by deed dated June 29, 1920, title to approximately

forty-seven (47) acres of real estate in the County of Los Angeles, as is more particularly described in the deed by which title was conveyed to Taxpayer, a copy of which deed is attached to this affidavit [47] and marked Exhibit "A". That said property referred to in said deed is for convenience hereinafter referred to as "Parcel 1".

That on or about the 30th day of April, 1921, Taxpayer acquired from one Pearl Holmgreen, by deed dated April 21, 1921, approximately four (4) acres immediately adjacent to and lying to the West of said Parcel 1, which real property is more particularly described in the deed by which said Taxpayer acquired said title, a copy of which deed is attached hereto and marked Exhibit "B", and the parcel of land therein described is hereafter described as "Parcel 2".

That thereafter, on or about the 11th day of March, 1922, Taxpayer acquired title from the Winter Investment Company, by deed dated February 8, 1922, to certain real property adjacent to said Parcels 1 and 2, and lying to the South thereof, which said property is more particularly described in said deed a copy of which is hereto attached and marked Exhibit "C". Said real property last mentioned is hereinafter referred to as "Parcel 3".

Use of Land.

That prior to the year 1920 Taxpayer was engaged [48] in the buying, from time to time, of lettuce and other Fall, Winter and Spring vege-

tables, in and about the vicinity of Los Angeles, California, for packing, shipment and sale. That the property above mentioned was located near Los Angeles in what is commonly called the "Montebello District". That such district was considered as one of the most favorable, if not the most favorable district within Los Angeles County for the raising of Fall and Winter vegetables, and particularly lettuce; and that Taxpayer, in purchasing and holding said real property, and all of it, purchased and held the same in order to raise thereon said Fall, Spring and Winter vegetable crops, and particularly lettuce. That said real property was never purchased or held by the Taxpayer primarily or at all for sale in the course of Taxpayer's trade or business, or otherwise.

That after acquiring said Parcel 1, Taxpayer immediately planted the same to lettuce, which was harvested during the succeeding year. That during the years 1921, 22, 23 and 24, and part of 1925, as rapidly as said real property described as Parcels 1, 2 and 3 were acquired, Taxpayer used and held the same, with the exceptions hereinafter noted, for the raising of lettuce exclusively, except as to the [49] year 1924, when a portion of said property was planted to endive or chicory.

That during the year 1921 Taxpayer erected buildings and other structures on not over three and one-half acres of said Parcels 1 and 2 and thereafter, up to the year 1930, used the same as a combined office and place of residence for Taxpayer.

Changing Character of Land.

That after Taxpayer acquired said real property, a great deal of real estate activity developed between such real property and the eastern boundary of the City of Los Angeles, and, beginning with said eastern boundary of the City of Los Angeles, the intervening property began to be subdivided, sold and developed, until such development reached the vicinity of the property owned by Taxpayer. That said property of Taxpayer, by reason of such development, and by reason of the fact that it fronted on the two main highways south from the City of Los Angeles to the southern part of the State of California, and the fact that the main highway from Pasadena, California, to Long Beach, California, was planned to run through a portion of said property said property increased in value very [50] rapidly to such an extent that it was unprofitable to use the same further for the raising of vegetable crops, being worth in excess of \$4000.00 per acre, without improvements, and the upkeep by way of taxes, assessments for local improvements and similar charges made the further holding of said property for farm purposes undesirable. That the amount of County Taxes paid by the Taxpayer on the portions of the real property held by him amounted to \$657.84 for the year 1920, to \$586.15 for the year 1921, to \$1410.53 for the year 1922, to \$3890.32 for the year 1923, to \$4758.49 for the year 1924, and to \$5903.22 for the year 1925. In addition, the Taxpayer was required to pay during the year 1924 the sum of \$4479.95 on account of special assessments

for local improvements charged against such property. That, therefore, during the year 1925, Taxpayer determined upon a subdivision and sale of a part of said Parcel 1.

Method of Subdivision.

That the system followed by the Taxpayer in subdividing and selling said property was not the "typical subdivision project" in that Taxpayer was not acquiring any property especially for sale, but Taxpayer was disposing of his own property, although the making of the actual sales was to be handled by [51] one P. N. Snyder, a real estate broker and agent, whose business was buying, selling and acting as an agent in the sale of real estate. That Taxpayer decided to convey a portion of the property in trust to the Security Trust & Savings Bank, of Los Angeles, California (now the Security-First National Bank of Los Angeles), in order that when Taxpayer was absent from the vicinity of Los Angeles the disposal of said real property could continue uninterrupted, and all bookkeeping and accounting connected with said sales could be handled by the said bank in an economical and systematic fashion. That before conveying said portion of said Parcel 1 in Trust, Taxpayer determined upon a subdivision of said property, the improvements to be installed in said property and upon the prices at which the same should be sold. That after determining upon such program for the improvement and sale of such portion of said Parcel 1, the Taxpayer executed a deed to said bank, and said

bank did execute an agreement agreeing to hold said property in accordance with the terms and provisions thereof and for the benefit of the Taxpayer. Such subdivision was designated as Tract No. 8790 and was made effective as a subdivision by the recording of the plat thereof by said bank after said trust had been created, to-wit: on the 10th day of September, [52] 1925; and Taxpayer did furnish to said bank a list of prices at which each and all of said lots should first be sold. That a copy of said trust agreement is hereto attached and marked Exhibit "D", and that a copy of said subdivision plat is likewise hereto attached and marked Exhibit "E". That said trust was known and designated by said bank as "Trust 2-1780".

That the sale of said lots in said Tract No. 8790 proving satisfactory to said Taxpayer, Taxpayer caused the remaining portion of said Parcel 1, all of Parcel 2, and a portion of Parcel 3 to be subdivided, improved, prices fixed and the property to be conveyed to said bank to be held in trust in the same manner as said Tract No. 8790, and did create a trust for the sale of the same, a copy of which trust is hereto attached and marked Exhibit "F" and is known and designated by said bank as "Trust No. 2-1850". That by reason of an error in the description of the deed by which the Taxpayer conveyed the real property constituting Track No. 8790 to said bank, said bank already held title to a portion of the property included in Trust No. 2-1850, but no agreement had been entered into with refer-

ence to the same. That said bank, after said trust had been created, and in accordance with the subdivision plan [53] previously determined on by Taxpayer, caused to be recorded on or about August 3, 1926, a subdivision map designated as Tract No. 9436, and a copy of said map is hereto attached and marked Exhibit "G".

That the Taxpayer did thereafter determine to subdivide and sell the remaining portion of said Parcel 3, and did thereafter in like manner cause a survey to be made of said property and determine upon a subdivision and improvement thereof, and did fix the sale prices and did create a trust with said bank, and did convey the balance of said Parcel 3 to said bank in such trust. That a copy of the trust agreement between the Taxpayer and said bank is hereto attached and marked Exhibit "H", and said trust was known by said bank as "Trust No. 2-1899". That after said trust was created such bank did, at the direction of the Taxpayer and in accordance with his program for subdivision theretofore determined on by Taxpayer, cause to be recorded in the County of Los Angeles a certain map on the 23rd day of February, 1927, whereby said tract was known as Tract No. 9797. That a copy of said Tract No. 9797 is hereto attached and marked Exhibit "I".

That audits have been made by the Internal [54] Revenue Service of the Treasury Department of each and all of said three trusts, and that said audits have determined the amount of profit from year to

year received by Taxpayer from each and all of said trusts. That Taxpayer has accepted as correct the amount of profit as determined by said audit received by the Taxpayer as the result of each and all of said trusts, but Taxpayer does not concede the correctness of the contention of the Internal Revenue Service as to the amount of tax Taxpayer should pay for the fiscal years 1926-27 and 28 by reason of the profits received by the Taxpayer from the sale of said real property in said three trusts with said bank, as aforesaid, nor the basis on which such taxes should be computed.

Business Carried on by Taxpayer.

That while Taxpayer was raising and selling lettuce on the real property above described as Parcels 1, 2 and 3, during the years 1920 to 1923, Taxpayer was engaged in the business of buying and selling lettuce outright, and during a portion of the time operating a packing house at 1014 Lawrence Street, Los Angeles. That during the year 1923, Taxpayer leased approximately three hundred and eighteen (318) acres of land in the Santa Maria Valley, in Santa Barbara County, California, and raised and sold lettuce thereon, and also leased seventy-two (72) [55] acres adjacent to Taxpayer's real property above described as Parcels 2 and 3, and raised, produced and sold lettuce therefrom. That since the year 1923 Taxpayer has operated continuously one or more packing houses, either at 1014 Lawrence Street, Los Angeles, California, or at Reseda, California, or at Guadalupe, California..

That during the year 1924 Taxpayer increased his leaseholdings in the Santa Maria Valley by one hundred and fifty (150) acres additional, farming all of the same to lettuce.

That during the year 1925, Taxpayer increased his holdings in the Santa Maria Valley to approximately five hundred and sixty (560) acres and continued the growing, selling and marketing of lettuce on Parcels 1, 2 and 3 during the period of time that the same were not being subdivided and/or sold.

That during the year 1926 Taxpayer bought fifty-five (55) acres of land in the San Fernando Valley, Los Angeles County, California, for the purpose of raising lettuce thereon in lieu of the property being subdivided and sold by the Taxpayer. That during said year Taxpayer continued the operation of acreage in the Santa Maria Valley, as theretofore raising and selling lettuce therefrom. That during this year [56] the Taxpayer, jointly with one M. C. Wahl and the M. M. Cobb Company, undertook the raising of lettuce and melons in Imperial Valley, in Imperial County, California. That likewise, from the years 1918 to 1926, Taxpayer was farming real property to the extent of about two hundred and fifty (250) acres and raising lettuce thereon in the vicinity of Duluth, Minnesota.

That during all of such time Taxpayer was operating, up to the year 1929, under the firm name and style of W. M. Watson & Co., with offices at Chicago, Illinois, selling and handling lettuce, and other farm products, and during the year 1926 Taxpayer sold

on consignment from the Land Department of the Duluth and Iron Range Railroad large quantities of lettuce and cauliflower.

That during the year 1927 Taxpayer acquired fifty-five (55) acres of additional land in the San Fernando Valley and continued the raising of lettuce on all lands owned by the Taxpayer in this valley. That Taxpayer continued the operation of about five hundred and sixty-eight (568) acres of land in the Santa Maria Valley for the raising and selling of lettuce therefrom. That the Taxpayer at this time formed the partnership of M. C. Wahl & Co. with M. C. [57] Wahl, and continued operations in Imperial Valley, and Taxpayer financed and handled the crops on commission basis on some two hundred and sixty-one (261) acres in and about Salinas, California. That in addition, Taxpayer, under the name and style of W. M. Watson & Co., continued the handling and selling of consigned goods at Chicago, Illinois, and Taxpayer leased and farmed one hundred and fifty (150) acres in Sequim, in the County of McClellan, in the State of Washington.

That during the year 1928, Taxpayer continued raising and selling farm vegetables in the San Fernando Valley and in the Santa Maria Valley on the same acreage, and continued to handle farm vegetables and products in Chicago under the name of W. M. Watson & Co. The operations of M. C. Wahl & Co. had extended in the Imperial Valley so that

during this year this partnership was raising for market, and marketing, approximately six hundred (600) acres of lettuce and canteloupe.

That during the year 1929 Taxpayer leased and farmed seventy-two (72) acres in the San Fernando Valley, California, in lettuce and planted in alfalfa the one hundred and ten (110) acres owned [58] by Taxpayer. That Taxpayer farmed approximately five hundred and seventy (570) acres in the Santa Maria Valley to carrots, cauliflower and other winter vegetables. That the co-partnership of M. C. Wahl & Co. increased its holdings on which it raised lettuce and canteloupe to approximately twelve hundred (1200) acres, and in addition, Taxpayer leased approximately three hundred and twenty (320) acres in and about Salinas, Monterey County, California, for the purpose of growing and selling lettuce therefrom.

That the operations of Taxpayer for the year 1930 are generally similar to those carried on in 1929, but on a slightly more extensive scale.

That at no time has Taxpayer ever purchased any real estate for subdivision and sale. That at the time Taxpayer determined upon the subdivision and sale of said Parcels 1, 2 and 3, Taxpayer did not intend to go into the real estate business or to purchase any additional property for subdivision and sale. That at all times Taxpayer has been largely engrossed with the business of raising, buying and selling Fall, Winter and Spring vegetables and has

devoted practically all of his time to such business. [59] That in the sale of lots in the three tracts above mentioned Taxpayer took no active part, but the promotion, advertising and sale of said lots was handled by the said P. N. Snyder, who conducted his advertising campaign in such a manner as to create the impression that he was the subdivider and developer of the property above described, to such an extent that the general public believed that the said P. N. Snyder was the owner thereof, and did not know that the Taxpayer had any interest in and to the same. That attached hereto and marked Exhibit "J" is a map showing Parcels 1, 2 and 3 as a whole and before the same were subdivided. That attached hereto and marked Exhibit "K" is another map, showing the manner in which the entire tract was subdivided.

(Signed) ROBERT JAMES RICHARDS.

Subscribed and sworn to before me this 20th day of October, 1930.

[Notarial Seal]

(Signed) MURIEL P. MONTGOMERY,
Notary Public in and for the County
of Los Angeles, State of California.

[60]

I, C. E. McDOWELL, by whom the foregoing Affidavit has been prepared and filed, do hereby certify that I prepared the same and that in part the facts therein contained are of my own knowledge, and as to the remainder of said facts I have

been furnished the same by the taxpayer; and that affiant believes that the facts herein stated are true.

(Signed) C. E. McDOWELL,
922 Security Title Insurance Bldg.,
Los Angeles, California.

Petitioner's Exhibit "A", attached to the foregoing affidavit, is in the words and figures as follows:

GRANT DEED

I, YSIDORA COUTS FULLER, a widow, in consideration of TEN and 00/100 Dollars, to me in hand paid, the receipt of which is hereby acknowledged, do hereby GRANT to ROBERT JAMES RICHARDS and ARABELLA GRACE RICHARDS, husband and wife, as Joint Tenants, with the right of survivorship, all that real property situated in the County of Los Angeles, State of California, described as follows:

All that certain portion of the Rancho Laguna, so-called, in the Rancho San Antonio, County of Los Angeles, State of California, described as follows:

Beginning at an iron pipe, set in the Southerly line of the Whittier Road, at the most Easterly corner of Lot Twenty-one (21), Rancho Laguna, and running thence along the Easterly line of said Lot Twenty-one (21), South twenty-six degrees (26°) eighteen minutes (18') twenty seconds (20'') [61] West, thirteen hundred eight and twenty-two hundredths (1308.22) feet to an iron pipe set at the most Southerly corner of said Lot Twenty-one (21);

thence along the Southerly line of said Lot Twenty-one (21) and Lot Twenty (20), North seventy-five degrees (75°) thirty-seven minutes (37') West thirteen hundred thirty-one and fifty-seven hundredths (1331.57) feet to an iron pipe set at a point six hundred sixty-four and forty-nine hundredths (664.49) feet, North seventy-five degrees (75°) thirty-seven minutes (37') West from the most Westerly corner of said Lot Twenty-one (21); thence North fourteen degrees (14°) twenty-three minutes (23') East twelve hundred eighty (1280) feet to an iron pipe set in the Southerly line of the Whittier Road, at a point six hundred sixty-four and forty-nine hundredths (664.49) feet North seventy-five degrees (75°) thirty-seven minutes (37') West from the most Northerly corner of said Lot Twenty-one (21); thence along the Southerly line of said Whittier Road, South seventy-five degrees (75°) thirty-seven minutes (37') East sixteen hundred one and eighty-two hundredths (1601.82) feet to the point of beginning.

The same comprising the Easterly part of Lot Twenty (20) and all of Lot Twenty-one (21) as delineated on a map entitled Map of the Rancho Laguna and thereon marked with the name of "Ysidora Coutts Fuller", said map being the map filed as Exhibit "A" in connection with the Referees' Report in Action No. B-25296 of the Superior Court of Los Angeles County, entitled Ysidora Coutts Fuller vs. Cave J. Coutts et al.

SUBJECT TO: Taxes for the fiscal year 1920-21
TO HAVE AND TO HOLD to the said grantees,
as Joint Tenants, with the right of survivorship.

WITNESS my hand this 29th day of June, 1920.

YSIDORA COUTS FULLER.

STATE OF CALIFORNIA,
COUNTY OF LOS ANGELES.—ss.

On this Eleventh day of September, 1920, before
me, [62] W. F. Cook, a Notary Public in and for
said County, personally appeared YSIDORA
COUTS FULLER, a widow, known to me to be the
person whose name is subscribed to the foregoing
instrument and acknowledged that she executed the
same.

WITNESS my hand and Official Seal.

[Notarial Seal]

W. F. COOK,

Notary Public in and for County of Los An-
geles, State of California.

COMPARED

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RECORDED AT REQUEST OF LOS ANGE-
LES TITLE INS. CO.

Sep 15 1920 at 8:30 A. M. in Book 7306, Page 332
of Deeds Records, Los Angeles County, Cal.

C. L. LOGAN, County Recorder.

I certify that I have correctly transcribed this
document in above mentioned book.

C. HUNTER,

Copyist, County Recorder's Office,

L. A. Co., Cal.

[63]

Petitioner's Exhibit "B", attached to the foregoing affidavit, is in the words and figures as follows:

GRANT DEED.

I, Pearl Holmgreen, a single woman: in consideration of TEN DOLLARS to me in hand paid, the receipt of which is hereby acknowledged, do hereby GRANT TO Robert James Richards and Arabella Grace Richards, husband and wife, as joint tenants; all that real property situate in the County of Los Angeles, State of California, described as follows:

Beginning at an iron pipe set in the Southerly line of the Whittier Road, at a point 664.49 feet North $75^{\circ} 37'$ West from the most Northerly corner of Lot 21, Rancho Laguna, and running thence South $14^{\circ} 23'$ West 1280 feet to an iron pipe set in the Southerly line of Lot 20, Rancho Laguna, at a point 664.49 feet from the most Westerly corner of said Lot 21; thence along the Southerly line of said Lot 20 North $75^{\circ} 37'$ West 138.06 feet to an iron pipe; thence North $14^{\circ} 23'$ East 1280 feet to an iron pipe set in the Southerly line of the Whittier Road; thence along the Southerly line of Whittier Road, South $75^{\circ} 37'$ East 138.06 feet to the point of beginning,—the same comprising a portion of Lot 20, as delineated on said Map, Exhibit "A", attached to the Final Decree in Partition in Action No. B-25,295 of the Superior Court of Los Angeles County, a certified copy of which Decree is recorded in Book 6387 of Deeds, page 1, Records of Los Angeles County, California, containing 4057 acres.

SUBJECT TO taxes for the fiscal year 1921-1922; TO HAVE AND TO HOLD to the said grantees in joint tenancy. [64]

WITNESS my hand this 21st day of April, 1921.
PEARL HOLMGREEN.

STATE OF CALIFORNIA,
COUNTY OF LOS ANGELES.—ss.

On this 21st day of April, 1921, before me F. H. Greene, a Notary Public in and for said County, personally appeared Pearl Holmgreen, a single woman; known to me to be the person whose name is subscribed to the foregoing instrument and acknowledged that she executed the same.

WITNESS my hand and Official Seal.

[Notarial Seal] F. H. GREENE,
Notary Public in and for the County of Los
Angeles, State of California.

COMPARED

DOCUMENT VAN VELDIR
BOOK TOWER

RECORDED AT REQUEST OF TITLE INSURANCE & TR. CO., Apr. 30, 1921, at 8:30 A. M. in Book 185, page 307 of Official Records, Los Angeles County, Cal.

C. L. LOGAN, County Recorder. [65]

I certify that I have correctly transcribed this document in above mentioned book.

M. CHICK,
Copyist, County Recorder's Office, L. A. Co., Cal.

Petitioner's Exhibit "C", attached to the foregoing affidavit, is in the words and figures as follows:

GRANT DEED.

(Code) Corporation.

WINTER INVESTMENT COMPANY,

of the City and County of Los Angeles, State of California, a corporation duly organized and existing under and by virtue of the laws of the State of California, and having its principal place of business in the City of Los Angeles, County of Los Angeles, and State of California **FOR AND IN CONSIDERATION OF THE SUM OF** Ten and no/100 Dollars, the receipt whereof is hereby acknowledged, does hereby **GRANT TO ROBERT JAMES RICHARDS and ARABELLA GRACE RICHARDS**, his wife, as joint tenants with right of survivorship.

ALL THAT REAL PROPERTY, described as follows, to-wit: All that certain portion of the Rancho Laguna, so called, in the Rancho San Antonio, County of Los Angeles, State of California, described as follows: Beginning at an iron pipe set in the Northerly line of Lot Twenty-three (23), Rancho Laguna, at a [66] point four hundred ninety-eight and eighty-five hundredths (498.85) feet North seventy-five degrees (75°) thirty-seven minutes (37') West from the most Easterly corner of said Lot Twenty-three (23), and running thence South fourteen degrees (14°) twenty-three minutes (23') West twenty hundred forty-four and sixty-

nine hundredths (2044.69) feet to an iron pipe set in the North Easterly line of Anaheim Telegraph Road at a point eight hundred forty-seven and thirty hundredths (847.30) feet South sixty-one degrees (61°) twenty minutes (20') forty five seconds (45'') East from the most Westerly corner of said Lot Twenty-three (23); thence along the North Easterly line of the Anaheim Telegraph Road North sixty-one degrees (61°) twenty minutes (20') forty-five seconds (45'') West eight hundred forty-seven and thirty hundredths (847.30) feet to an iron pipe at the most Westerly corner of said Lot Twenty-three (23); thence North fourteen degrees (14°) twenty-three minutes (23') East along the Westerly line of said Lot Twenty-three (23) eighteen hundred thirty-five and eighty-three hundredths (1835.83) feet to an iron pipe set in the Northerly corner of said Lot Twenty-three (23); thence along the dividing line between Lots Twenty (20) and Twenty-three (23) South seventy-five degrees (75°) thirty-seven minutes (37') East eight hundred twenty-one and fifteen hundredths (821.15) feet to the point of beginning. The same comprising the Westerly portion of Lot Twenty-three (23), as delineated on a map entitled "Map of the Rancho Laguna" and thereon marked with the name of "John F. Coutts", said map being the map filed as Exhibit "A" in connection with the Referee's Report in Action No. B-25,296 of the Superior Court in Los Angeles County, entitled Ysidora Coutts Fuller v. Cave J. Coutts, et al., and attached to Final Decree of Partition of said Action, a certified copy

of which decree is recorded in Book 6387, page 1 et seq., of Deeds in the office of the County Recorder of said County.

IN WITNESS WHEREOF, the said party of the first part has caused its corporate name and seal to be affixed by its President and Secretary thereunto, duly authorized this 8th day of February, nineteen hundred and twenty-two.

[Corporate Seal] WINTER INVESTMENT
 COMPANY,
 By GEORGE F. WINTER,
 President,
 By FRANK C. WINTER,
 Secretary. [67]

STATE OF CALIFORNIA,
COUNTY OF LOS ANGELES.—ss.

On this 10th day of February, A. D., 1922, before me, Margaret F. Brennan, a Notary Public in and for the said County and State, residing therein, duly commissioned and sworn, personally appeared George F. Winter known to me to be the President and Frank C. Winter known to me to be the Secretary of the Winter Investment Company the Corporation that executed the within Instrument, known to me to be the persons who executed the within Instrument, on behalf of the Corporation therein named, and acknowledged to me that such Corporation executed the same.

IN WITNESS WHEREOF, I have hereunto set my hand and affixed my official seal the day and year in this certificate first above written.

[Notarial Seal] MARGARET F. BRENNAN,
Notary Public in and for said County and State.

COMPARED

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RECORDED AT REQUEST OF TITLE INSURANCE & TR. CO., Mar. 11, 1922, at 8:30 A. M. in Book 963, page 92 of Official Records, Los Angeles County, Cal.

C. L. LOGAN, County Recorder.

I certify that I have correctly transcribed this document in above mentioned book.

C. FLETCHER,

Copyist, County Recorder's Office, L. A. Co., Cal.
[68]

Petitioner's Exhibit "D", attached to the foregoing affidavit, is in the words and figures as follows:

DECLARATION OF TRUST.

Trust No. 2-1780.

THIS DECLARATION OF TRUST, made and entered into as of the 15th day of July, 1925, by and between ROBERT JAMES RICHARDS and ARABELLA GRACE RICHARDS, husband and wife, of Los Angeles County, California, parties of the first part, hereinafter sometimes referred to as "Trustors", "Payor" and also as "Beneficiary", SECURITY TRUST & SAVINGS BANK, a cor-

poration of Los Angeles, California, party of the second part, hereinafter sometimes referred to as the "Trustee", and SECURITY TRUST & SAVINGS BANK, as party of the third part, hereinafter sometimes referred to as "Payee".

WITNESSETH:

WHEREAS, the Beneficiaries hereunder are now indebted to the Payee herein in the principal sum of \$28,500.00, which indebtedness is evidenced by a certain promissory note, dated June 11, 1925, made and executed by the said Beneficiaries in favor of said Payee and delivered by said Beneficiaries to said Payee and which promissory note is in words and figures as follows, to-wit:

\$28,500.00 Los Angeles, Cal. June 11, 1925.

On or before December 11th, 1927, for value received, I promise to pay to the SECURITY TRUST & SAVINGS BANK, Guaranty Office, Los Angeles, California, the sum of TWENTY-EIGHT THOUSAND FIVE HUNDRED and 00/100 (\$28,500.00) DOLLARS, with interest thereon from date, until paid, at the rate of six and one-half per cent ($6\frac{1}{2}\%$) per annum, payable quarterly, and should the interest not be so paid it shall bear like interest as the principal. And if any installment of interest herein is not paid when due, or in case of failure to comply with any of the conditions of the Trust Agreement by which this note is secured, the principal and accumulated interest thereon shall become due and collectible at once or at any time thereafter during such delinquency, without notice,

at the option of the holder of this Note. Principal and interest payable in United States gold coin. Privilege is reserved to make partial payments at any time in multiples of ONE THOUSAND and 00/100 (\$1000.00) DOLLARS on the principal of this note. This note is secured by Declaration of Trust No. 2-1780 with the SECURITY TRUST & SAVINGS BANK, a corporation.

ROBERT JAMES RICHARDS,
ARABELLA GRACE RICHARDS. [69]

The Trustee hereunder shall be under no obligation as to the payment of either the principal or the interest due under the terms of said note, except as to the application thereto of the moneys coming into its hands for that purpose as hereinafter provided.

WHEREAS, by deed dated July 15th, 1925, and recorded August 21st, 1925, in the office of the County Recorder of Los Angeles County, Robert James Richards and Arabella Grace Richards, husband and wife, did convey to the Security Trust & Savings Bank, a corporation and do hereby grant to the Security Trust & Savings Bank, with power of sale, all that real property situated in the County of Los Angeles, State of California, described as follows:

“All that portion of the Rancho Laguna, so-called in the Rancho San Antonio, County of Los Angeles, State of California, described as follows:

Beginning at an iron pipe set in the Southerly line of the Whittier Road at the most Easterly

corner of Lot Twenty-one (21), Rancho Laguna, and running thence along the Easterly line of said Lot Twenty-one (21), South Twenty-six degrees (26°) eighteen minutes ($18'$) twenty seconds ($20''$), West thirteen hundred eight and twenty-two hundredths (1308.22) feet to an iron pipe set at the most Southerly corner of said Lot Twenty-one (21); thence along the southerly line of said Lots Twenty-one (21) and Twenty (20), North seventy-five (75°) degrees thirty-seven minutes ($37'$) West eleven hundred thirty-one and fifty-seven hundredths (1131.57) feet to an iron pipe set at a point six hundred sixty-four and forty-nine hundredths (664.49) feet, North seventy-five degrees (75°) thirty-seven minutes ($37'$) West from the most Westerly corner of said Lot Twenty-one; thence North fourteen degrees (14°) twenty-three minutes ($23'$) East twelve hundred eighty (1280) feet to an iron pipe set in the Southerly line of the Whittier Road, at a point six hundred sixty-four and forty-nine hundredths (664.49) feet north seventy-five degrees (75°) thirty-seven ($37'$) minutes West from the most northerly corner of said Lot Twenty-one (21); thence along the Southerly line of said Whittier Road, South seventy-five degrees (75°) thirty-seven minutes ($37'$) East sixteen hundred one and eighty-two hundredths (1601.82) feet to the point of beginning. [70]

The same comprising the Easterly part of Lot Twenty (20), and all of Lot Twenty-one (21) as delineated on a map of the Rancho Laguna and

thereon marked with the name "Ysidora Coutts Fuller", said map being the map filed as Exhibit "A" in connection with the Referees' Report in Action No. B-25,296 of the Superior Court in Los Angeles County, entitled Ysidora Coutts Fuller v. Cave J. Coutts et al."

and as shown by Guarantee No. 607,622, of the Title Guarantee and Trust Company, dated August 21, 1925, at 8:30 A. M., the title to all property was on said date vested in the

"SECURITY TRUST & SAVINGS BANK,
a corporation,

Free of incumbrances

EXCEPT: Taxes for the fiscal year 1925-26."

WHEREAS, no consideration was paid by the Security Trust & Savings Bank for such conveyance, and while such conveyance was in form, and by its terms absolute, yet nevertheless, the same was intended to be and was received by the said Trustee herein in trust, with power of sale, primarily for the purpose of subdividing, renting, leasing, selling and conveying said property in accordance with the terms and conditions hereinafter set forth.

AND, also, said conveyance has been received for the purpose of securing the repayment of the note now owing from the said Beneficiaries to the said Payee herein, as hereinbefore set out, which indebtedness it is hereby declared and admitted, is a first lien upon the Trust property, together with

all interest that may be due or that may accrue on said note, together with any renewals of said note.

AND, also as security for the payment of any additional sums, with interest thereon, that may be hereafter borrowed and received by the said Beneficiaries from said Payee and from Trustee and evidenced by another promissory note or notes executed and delivered by said Beneficiaries to said Payee and/or Trustee, together with any renewal or renewals of said notes and also as security for any sums of money with interest thereon, that may be expended either by the Trustee or Payee hereunder as hereinafter provided.

NOW THEREFORE, THIS DECLARATION
OF TRUST

WITNESSETH: [71]

THAT, the Security Trust & Savings Bank does hereby certify and declare that it holds and shall hold all of the interest in said property conveyed to it through said conveyance in Trust, with power of sale, for the purpose of securing the payment on the above described indebtedness or promissory notes and also for the purpose of renting, leasing, selling and conveying the said property and applying and disposing of the proceeds and avails arising therefrom, in accordance with the terms and conditions herein expressed, to-wit:

ARTICLE FIRST: During the continuance of these trusts the Beneficiary agrees as follows:

(a) To pay before delinquency all taxes and assessments levied and assessed against and upon the property covered hereby and/or against the debt secured hereunder during the life of the Trust.

(b) To pay the principal and interest of any indebtedness and on said notes secured hereby, as and when due.

(c) To pay, when due, all other claims, liens and encumbrances affecting, or purporting to affect, the title to the property covered hereby, and all costs, charges, interest and penalties on account thereof; and also all costs, fees, charges and expenses of the Trustee and of these Trusts.

(d) To appear in and defend or cause to be defended any action or proceeding at law affecting, or purporting to affect, the property covered hereby, these trusts, or the rights of either the Trustee or the Payee hereunder; and the said Beneficiary hereby agrees to pay all costs and expenses of any such action or proceeding, together with attorneys' fees in a reasonable sum to be fixed by the Court whether any such action or proceeding progress to judgment or not, and whether brought by or against the Trustee or the Payee hereunder.

(e) To protect, preserve and defend said property and the title thereto, and to keep said property in good condition, by proper care, inspection, repair, cultivation, irrigation, fertilization or otherwise, and to permit no waste or deterioration thereof, and also to pay for all improvements contracted for or ordered by the said Beneficiary or his agent.

(f) To file with the Trustee a copy of such contract let for any improvements to be placed on each unit of the Trust property as subdivided, and any such improvements placed upon the Trust property will be superintended by the Agent, hereinafter appointed. [72]

(g) In the event the Beneficiaries shall fail to put in and pay for the improvements promised and guaranteed by them or their agents to the purchasers of lots or parcels of property in this Trust, the Trustees shall have the authority, and is hereby given express authority, to contract for and to have installed upon the property all or any of said improvements so promised and guaranteed by the Beneficiaries, and for the purpose of paying for said improvements, is hereby given the further authority and right to impound sufficient funds out of the moneys coming to it under this Trust belonging to the Beneficiaries to pay for the said improvements so contracted, either by the Beneficiaries or by the Trustee on behalf of said Beneficiaries.

The Beneficiaries agree to file with the Trustee specifications covering the improvements so promised by them or their agents and should the Beneficiaries fail so to do, the Trustee is hereby given the authority to contract and pay for improvements, which in its sole discretion, shall appear to said Trustee to meet the promises of the Beneficiaries or their agents as set forth either in the printed matter of the Beneficiaries or their agents or from

evidence presented to the Trustee by purchasers of said Trust property.

(h) The Trustee shall not be required to issue any deed or contract until said Beneficiaries have filed with the Trustee a copy of each such contract as called for in paragraph (f) herein.

(i) The said Beneficiaries agree to file with the Trustee a copy of all of the advertising and printed matter used by them or their agents in connection with the sale of the Trust property, and also a form of the receipt given to the purchasers for any moneys received by them in connection therewith; also a copy of any promises and representations made by themselves or their agents as to improvements to be placed upon the Trust property, and as to any representations to their purchasers as to any re-sales to be made by them, and also which they may permit their sub-agents to make and represent to their purchasers.

(j) To repay, within Thirty (30) days from the date of advancement, and without demand, all sums advanced or expended by the Trustee or the Payee under the terms hereof, with interest thereon from the date of advancement until repaid at the rate of seven per cent (7%) per annum. Should said Beneficiary fail or refuse to make any of the payments, or do any of the acts in the manner and at the times above provided, then the Trustee and/or the Payee, without notice to the Beneficiary, may make or do the same in such manner and to such extent as they, or either of them may elect, and

to that end, said Trustee and/or said Payee may enter and take possession of said property at such times and for such period or periods as they or [73] either of them may deem necessary and/or proper; and said Trustee and/or payee may pay, purchase, contest or compromise any claims, liens or encumbrances which in their judgment or the judgment of either of them appear to affect said property or these trusts, and may advance money or moneys from time to time, for any payment or purpose whatsoever in connection with this Trust; it being distinctly understood however that neither the Trustee, nor the Payee shall be under any obligations to do any of the things mentioned above.

Upon failure of the Beneficiaries to re-pay to the Trustee and/or the Payee any sums advanced by them as herein provided for, together with interest thereon at the time and in the manner as herein specified, such act shall constitute a default hereunder and subject the Beneficiaries to a sale of their rights hereunder as provided in Article Sixteenth herein.

ARTICLE SECOND: The real property covered hereby is to be subdivided and the same shall be improved by the Beneficiary hereunder in such manner as shall be agreed upon by said Trustee and said Beneficiary.

ALL COSTS and expenses, however, incident to such subdivision and improvements shall be borne solely by said Beneficiary, and no part thereof shall be borne by said Trustee or the Payee hereunder.

AND said beneficiary, by his approval of this Declaration, also does promise and agree to protect and save harmless said Trustee and the Payee hereunder from all loss, damage, liability, and expense, by reason of such subdivision and improvements of the trust property and likewise does promise and agree to furnish to the Trustee and the Payee, prior to incurring any obligations in connection with such subdivision and improvements, bond or bonds in substance and in form approved by the Payee, protecting and indemnifying the Trustee and the Payee from all loss, damage, liability and expense, by reason of the subdivision and improvements of the trust property.

ARTICLE THIRD: The Trustee shall rent, lease, sell or convey said property, or any portion thereof and/or the lots in any subdivision thereof, to such person or persons, at such prices and upon such terms and conditions as said Trustee shall deem advisable. PROVIDED that the sales prices of said lots shall not be less than those indicated on the schedule of Minimum Sales Prices hereafter to be agreed upon by said Trustee and the Beneficiary hereunder, copy of which Sales Prices shall be attached hereto and shall be a part hereof. [74]

ARTICLE FOURTH: All proceeds received by said Trustee, arising from each sale made hereunder of any lot or lots in said subdivision or from the rents, leases and sales of said property shall be disbursed and distributed as follows:

1. As to sales made for cash the Trustee shall credit:

(a) To a "Commission Fund" twenty-two and one-half ($22\frac{1}{2}\%$) per cent of the sales price of each lot so sold as commission due the Agent hereunder.

(b) To a "Release Fund" the amount necessary to release the lots so conveyed by the Trustee from the lien in favor of the Payee hereunder.

(c) The balance to the "General Fund".

2. As to sales made for other than all cash the Trustee shall credit each initial cash or down payment received upon issuance of contract and each payment of principal thereafter received.

(a) $\frac{1}{3}$ thereof to the "Commission Fund" until the commission due the Agent for the lots so sold shall have been paid in full, and

(b) $\frac{2}{3}$ to the "General Fund".

3. All interest received on Agreement of Sale shall be credited to the "General Fund".

4. The moneys in the "Commission Fund" shall be disbursed monthly by the Trustee to the Agent hereunder.

5. Out of the money credited to the "General Fund" the Trustee shall pay:

(a) The costs, fees and expenses and advancements (if any) with interest, hereunder of said Trustee.

(b) Either before or after delinquency, all taxes and assessments, both general and special, levied, assessed or imposed on or against said property or payable by the purchaser thereof from the Trustee.

Should the money in the hands of the Trustee available for that purpose be insufficient to pay said taxes or assessments when due, then the Beneficiary, by his ratification of this declaration of trust, covenants and agrees to immediately pay to the Trustee any deficiency in the amount due on said taxes and assessments. [75]

(c) Interest on the indebtedness secured hereby unless the same shall have been otherwise paid.

(d) All bills for labor incurred and materials furnished for the improvement of said property, upon the approval thereof by the Beneficiary or Leeds & Barnard, as his engineers, or any other person designated by him.

(e) Interest on unpaid commissions of the agent as hereinafter provided.

(f) To the principal of the indebtedness evidenced by the note above mentioned or any other note or indebtedness secured hereby.

(g) And the remainder thereof not otherwise required for the purposes of this Trust to the said Robert James Richards and Arabella Grace Richards as joint tenants, Beneficiaries hereunder, upon the death of either, payments to be made to the survivor.

ARTICLE FIFTH: The Trustee at the request of the Beneficiaries hereunder appoints P. N. Snyder, of Los Angeles, California, as their exclusive agent to subdivide and improve, and to solicit and obtain purchasers for such part of said property of which a subdivision map shall have been

filed and designated herein as Unit No. 1, and to generally assume the care and custody thereof.

ALL SALES to be made by said agent shall be for prices not less than those indicated on the "Minimum Sales Price List" to be attached hereto and upon the following minimum terms:

25% of the actual sale price in cash at date of sale and the balance in monthly installments in an amount equal to not less than 2% of the actual sale price, and interest on the unpaid balance at the rate of 7% per annum, payable quarterly.

A discount of 5% may be allowed if the purchase price is paid all in one payment in cash, or a discount of 5% of the balance due on the purchase, if such balance due shall be more than 60% of the purchase price and be paid in one cash payment, and a 5% building discount shall be paid to any cash purchaser of a lot at such time that a building thereon shall have been completed to the extent of the roof having been placed thereon within ninety days from the date of execution of the deed to such lot.

The Beneficiaries and Trustee reserve the right to withdraw from sale, certain lots in said Unit No. 1 not to exceed eighteen in number and of their own selection. [76]

AND each sale shall be subject to such conditions, restrictions and/or reservations and covenants as the said Trustee shall deem advisable.

No sale shall be made with any express or implied warranty or promise as to improvements to

be made except as those specifically agreed upon by the Trustee and as set forth in the copy filed with the Trustee provided for under paragraph (i) of Article First.

This Agency appointment shall be for a period of eight (8) months from the date hereof, but if the aggregate value of the lots sold in said subdivision either in cash or under contracts of sale issued by the Trustee hereunder before the expiration of said term of eight months shall equal one-half of the total aggregate value of all the lots in said subdivision as shown by the Minimum Schedule of Selling Prices to be hereto attached and herein referred to, then Agent may, at his option, by written notice to the Trustee and Beneficiaries prior to the expiration of said term of eight months extend the term of his appointment for a further period of eight months.

In the event of the cancellation or revocation of this appointment the Trustee shall appoint such Agent or Agents as the Beneficiaries may direct, or may rent, sell, lease or convey said property to such person or persons and upon such terms as the Beneficiaries hereunder may direct. All sales of said property, however, shall be subject to the approval of the Trustee.

The said Agent shall assume the general care and custody of the subdivided unit, including this supervision of all the improvements to be placed upon the Trust property, which said improvements shall include the installation of gas, water and electricity.

The said Agent is to be paid a commission of 22½% of the net sale price of each lot, (which shall be the gross price less all discounts allowed and not including any interest thereon), and said commission shall be paid in the manner and at the times as in this trust agreement provided.

In addition thereto, said Agent shall receive interest at the rate of 7% per annum on respective unpaid commissions from the date that respective purchasers have begun to pay interest until said unpaid commissions are fully paid or said sale cancelled.

The agent shall pay out of his commissions for the advertising of the Trust property, selling expenses and his sub-agents commissions. [77]

The sale of each lot shall be considered separately, and the receipts from that sale will be used to pay commissions solely upon said sale.

It is understood and agreed that the Trustee hereunder shall not be liable to the Beneficiaries nor to any other person for any default, defalcation or wrong-doing of the said Agent or its sub-agents.

For any service rendered by said agent under this appointment, it shall be entitled only to such commissions as are herein set forth, and in any event, it shall be entitled only to the payment to it of the proportionate amount of the moneys actually paid in by any purchaser under any agreement of sale, or other evidence of sale and purchase in accordance with the agreed upon manner of distribution, and that no charge or claim shall be

made upon the SECURITY TRUST & SAVINGS BANK, Trustee, for any portion of the unpaid commissions payable from uncollected installments owing by any such purchaser; and this Trustee, at its discretion, and for any cause whatsoever, without liability to said agent for the balance of the unpaid commission, may cancel, annul or compromise any agreement of sale theretofore executed by it upon any portion of the foregoing described lands, the right of said agent to a commission for such sale to cease upon any such cancellation, annulment, rescission or compromise.

The said agent agrees to make a diligent and business-like effort to sell the said property as subdivided, and agrees to advertise the same at such times and in such manner as to create a material assistance in the selling of said property, and to pay for all such advertising.

Agent agrees to hold Trustee and Beneficiaries harmless from all loss, damage or claim arising from injury to persons or property and/or out of misrepresentation or alleged misrepresentation in their acts under the agency hereby created, and hereby agrees to save and hold Trustee and Beneficiaries harmless from all loss, damage or claim arising out of any default, defalcation or wrongdoing of themselves or of their salesmen or sub-agents.

The Agent agrees that nothing herein contained is intended to, nor shall it be construed as conferring any authority on Agent to execute deeds or

contracts to sell said lots, or to enter into contracts in the name of Trustee except temporary reservation contracts, or to incur liabilities on behalf of Trustee and Beneficiaries; and Agent expressly agrees that, except as to such temporary reservation contracts, they will enter into all contracts and incur all liabilities in their own names and [78] behalf only, and not in the name or on the behalf of Trustee and Beneficiaries.

P. N. Snyder, hereinbefore appointed agent, by his acceptance of this Declaration of Trust, accepts the agency hereby created, subject to all the terms and conditions as herein set forth.

ARTICLE SIXTH: The purchaser of each lot, or lots, sold hereunder from January 1st to June 30th of any year shall pay all taxes for the year in which the property was sold and thereafter. The purchaser of each lot, or lots, sold from July 1st to December 31st of any year, shall pay the second half of taxes for the year in which the property was sold and thereafter. All taxes for the fiscal year 1925-26 shall be pro-rated by the said Beneficiary.

ARTICLE SEVENTH: The Trustee shall execute all Agreements of Sale, Deeds and other instruments in writing, whatsoever requisite and necessary for the renting, leasing, transferring or conveying of said property or any portion thereof. Such Agreements of Sale and Deeds shall be subject to conditions, restrictions, reservations and rights of way of record, if any, and shall also con-

tain conditions and restrictions as shall be directed by the said Beneficiary and agreed to by the Trustee, and shall be subject to any and all ordinances of any city in which the property is located, or by any governmental or public agency creating or dealing with zones and prescribing the classes of buildings, structures and improvements in said zones and the use thereof.

The Trustee shall be under no liability or responsibility to the Beneficiary hereunder, nor to any other person, for the validity of any condition or restriction inserted in any Agreement of Sale or Deed, nor shall the Trustee be called upon to defend any suit, proceeding or action at law or in equity, to enforce the performance of, or enjoin the breach of, any such condition, restriction or ordinance, although the said Trustee may defend or prosecute such action at its election, and upon the request of the said Beneficiary, or any other person, and upon being indemnified for its costs and expenses in any such suit or suits.

ARTICLE EIGHTH: The said Trustee shall not be required to attend to or procure any insurance upon any building upon said property, or to collect or disburse any rents thereof, so long as this Trust shall continue, but all such services shall be performed and the expenses thereof borne by the said Beneficiary or his representatives.

ARTICLE NINTH: During the continuance of these Trusts the Trustee is authorized to pay: taxes levied and assessed against said property; any spe-

cial assessment levied against said property or any portion thereof, of which the Trustee shall receive due notice; any other liens or charges against said property necessary for the preservation or maintenance thereof, but all of the above mentioned payments shall be at the expense of the Beneficiary hereunder, and the said Beneficiary, by his ratification of this Declaration of Trust, covenants and agrees to pay to the said Trustee sufficient moneys with which to pay the same before the same becomes delinquent.

ARTICLE TENTH: The Trustee reserves unto itself the right, and shall have the power, solely within its discretion for the benefit of the Beneficiary hereunder, to replace, renew or extend any debt or incumbrance upon the Trust property, or any part thereof, when the same becomes due or at any time such replacement, renewal or extension may be in the judgment of said Trustee for the best interests of this Trust or necessary to protect the Trust property; and upon such terms and upon such conditions and by such means of security as said Trustee may deem proper, including the right and power to convey the fee title to said property, or any part thereof, to such person or corporation as it shall select for the purpose of executing and delivering the necessary note, mortgage, deed of trust, or other hypothecation, to evidence and secure such debt or debts and of reconveying said property to said Trustee subject thereto, and when such reconveyance shall have been so made, said Trustee shall thereupon be restored to its full estate hereunder.

It being distinctly understood that any such conveyance by said Trustee, for the purposes hereinabove stated, shall in no wise be construed as a suspension or termination of this Trust or as in any way impairing, changing or limiting the powers of the said Trustee, as herein expressed and intended. But the powers conferred by this Article shall not be exercised by the Trustee unless the Mortgagees and the Payee hereunder shall have been paid in full, except with their written consent.

ARTICLE ELEVENTH: The Trustee shall not be obligated to convey to the said Beneficiary, nor to any other person, any land covered by any existing Agreement of Sale, so long as such Agreement is in force and effect, but shall be and is hereby authorized to retain the title to all of said land covered by such Agreement until said Agreement has been paid in full by the holder thereof, and the land shall then be deeded to the holder of said Agreement in accordance with the terms thereof; nor shall the Trustee be obligated to convey, upon the order of the Beneficiary hereunder, or upon the order of any party to this Trust, any property upon which an Agreement to Convey has been cancelled, until time as a cancellation thereof has been effected in form satisfactory to the said Trustee.

[80]

It is understood and agreed however, that the Trustee, upon being indemnified by the Beneficiary for its costs, fees and expenses, shall upon request of the said Beneficiary, take such legal action as may be necessary for the enforcement of the terms

of any of the Agreements then outstanding and in default, or take such legal action as may be necessary to obtain a Court Decree quieting its title or obtain such other acquittance as is satisfactory to the Trustee, to any portion of the Trust property upon which an Agreement to Convey has been, or is to be, forfeited, provided that the purchaser's unrecorded copy of such Agreement has not been surrendered to the Trustee for cancellation, but all at the cost and expense of the said Beneficiary.

ARTICLE TWELFTH: The Trustee does not, either as Trustee or in any other capacity, assume or guarantee the payment of the indebtedness secured hereby, or any part thereof, nor does it guarantee the performance, in whole or in part, of any Agreement of Sale made hereunder by the purchaser thereunder.

It is further understood that the provision relating to the payments to be made by the Trustee shall not be construed so as to impose any obligation upon the said Trustee, unless there shall be, at the time such payment becomes due, sufficient moneys in the hands of the Trustee belonging to this Trust to enable it to make such payments.

ARTICLE THIRTEENTH: The costs, fees and expenses of the Trustee hereunder are hereby fixed as follows:

First: For accepting this Trust and executing this Declaration, a sum equal to one-tenth of one per cent ($1/10$ of 1%) of the gross selling price of said property.

Second: Two per cent (2%) of the gross sales price of any lot or lots where the sales price shall all be paid on one cash payment.

Third: Three per cent (3%) of the gross sales price which includes interest thereon of any lot or lots where the sales price shall be paid in deferred payments, and three per cent (3%) on all other sums collected under the provisions of this Trust Agreement.

PROVIDED, however, that the aggregate [81] compensation under items two and three shall not be less than TWO HUNDRED FIFTY (\$250.00) DOLLARS per year.

Fourth: Two and 50/100 (\$2.50) Dollars per lot for each Contract in duplicate, and Two and 50/100 (\$2.50) Dollars per lot for each Deed executed by said Trustee.

Fifth: The necessary cost of Revenue Stamps, guarantees of title, recording charges, escrow charges, the cost of printing forms of Agreements of Sale and Deeds, and any other charge or expenses necessary to consummate the sales of the property.

Sixth: A reasonable compensation for any service rendered by said Trustee in the execution of this Trust for which the costs, fees and expenses are not herein provided, and including a reasonable compensation (in addition to the counsel fees and other expenses) for any service rendered under this Trust by the said Trustee in connection with any action or proceeding at law (including any arising from the death of any Beneficiary hereunder), or

in paying or attending to the payment of any taxes or assessments in connection with any income tax, inheritance tax or estate tax matter affecting the Trustee, any Beneficiary hereunder, or the Trust property or any portion thereof.

Mortgages or trust deeds given by purchasers to the Beneficiary, or assigned to the Beneficiary, to cover principal payments, are, for purposes of determining fees, to be treated as cash payments, but if held by the Trustee and under the same terms as Agreements to Convey, the regular collection fee as herein stated will be charged.

ARTICLE FOURTEENTH: The said Beneficiary, by his ratification of this Declaration of Trust, covenants and agrees to hold and save harmless the Trustee hereunder from any and all liability, claims, demands, injuries or damages which it may suffer or sustain by reason of the acceptance of this Trust, and its position as Trustee hereunder, and to protect said Trustee from any loss, damage, cost or expense by reason of the improvements of any character whatsoever made on said property, and [82] against all expenses incurred by any Agent of the Beneficiary or any Agent appointed by the Trustee at the request of the Beneficiary in the handling or sale of said property, and, upon demand of the Trustee, to furnish said Trustee with such further guaranty or indemnity as said Trustee shall deem necessary to protect said Trustee and said lands against any loss, damage, cost or expense by reason of such sale or improvements.

ARTICLE FIFTEENTH: If the whole or any portion of the interest of the Beneficiary hereunder, or any Beneficiary, if there be more than one Beneficiary, or the Mortgagees or the Payee hereunder, or the proceeds or avails of any such interest, shall, at any time during the terms or upon the expiration of this Trust, become liable for payment of any estate, inheritance income or other tax, charge or assessment which said Trustee shall be required to pay, then unless such taxes shall have been fully paid when due, by someone else, said Trustee is hereby authorized without previous notice to or demand upon any person, to pay such taxes out of the whole or any portion of the interest so affected, and for that purpose of hereby generally and specifically authorized and empowered, without previous notice or demand to or from any person whomsoever, to sell at public or private sale, and convey sufficient portion of such interest up to the whole thereof as shall fully pay all such taxes, all costs and expenses of such sale, all the sums, together with interest thereon at Seven per cent (7%) per annum, payable quarterly, then due the Trustee under this Trust or which it may have advanced or expended in the care, management and protection of the Trust Estate and in the payment of any said estate, inheritance, income or other taxes therein, and which said Trustee may be required to pay. Until such sums have been fully paid, they shall constitute a first lien on all the property subject to this tax, and in favor of said Trustee.

ARTICLE SIXTEENTH: If default be made in the payment of principal or interest of said debt secured hereby, or in the payment of principal or interest of any other sum or amount properly payable under this Trust, by the sole Beneficiary hereunder, or by the Beneficiaries if there then be more than one, or upon breach by said Beneficiary or Beneficiaries of any covenant, condition or stipulation hereof, then the party or parties (i. e. Payee and/or Trustee, as the case may be) as to whom such default or breach shall have been made may declare ALL SUMS secured hereby immediately due and payable and shall execute and deliver to the Trustee hereunder a written declaration of default and demand for sale, and after ninety (90) days shall have elapsed following the receipt thereof by said Trustee, but without the necessity of demand on any Beneficiary hereunder or any other person, said Trustee shall sell the entire beneficial interest under this Trust (i. e. the entire interest under this Trust of the sole Beneficiary, or the entire interest under this Trust of all Beneficiaries hereunder if there then be more than one), or such portion of said [83] entire beneficial interest (i. e. a portion of the interest under this Trust of the sole Beneficiary, or a proportionate amount of each interest under this Trust of each Beneficiary if there then be more than one Beneficiary hereunder) as may be necessary to pay said sums together with the expenses and Trustee's fees hereinafter mentioned.

SAID SALE shall be made in the following manner, namely:

Said Trustee first shall publish notice of the time and place of such sale with a description of the beneficial interest to be sold at least once a week for three (3) successive weeks, in a newspaper published in said City of Los Angeles, and from time to time may postpone such sale by publication in the same newspaper, or, at its option, by public announcement thereof at the time and place of sale so advertised; and, at the time and place of sale fixed as hereinbefore provided, said trustee may sell the beneficial interest so advertised or such portion as may be necessary to pay said sums, together with the expenses and Trustee's fees hereinafter mentioned, at public auction to the highest bidder for cash in United States gold coin and the Trustee, any Payee, or any person on behalf of either, or any other person, may bid and purchase at such sale, and upon such sale and after due payment made to it, said Trustee shall make and deliver to the purchaser at such sale an assignment of beneficial interest so sold; but without covenant or warranty, express or implied, regarding the ownership thereof or the taxes or other encumbrances thereon; whereupon such purchaser shall have all of the rights and privileges of the original Beneficiary or original Beneficiaries hereunder which property pass with said Assignment, subject, however, to all of the terms, conditions, and obligations of this Trust, but freed from lien of the debt mentioned as being secured by said Beneficial interest, and freed from the liens of all subordinate and inferior debts against the same.

Distribution of the proceeds received by said Trustee arising from each such sale shall be made by it as follows:

1st: To the payment of all expenses of such sale, including posting (if any) and advertising, and the costs, fees, charges and expenses of this Trust; also Trustee's fee for making such sale hereby fixed at Ten Hundred Dollars (\$1000.00) all in said gold coin; which said amounts shall all become due and payable upon receipt by said Trustee of written declaration of default and demand for said aforesaid.

2nd: To the payment of all sums which may have been advanced by said Trustee or any Payee hereunder—and not repaid—for the preservation, maintenance or protection of the property covered hereby, the title thereto, or any beneficial interest hereunder; together with accrued interest thereon.
[84]

3rd: To the payment of the amount then remaining unpaid of the hereinbefore described debt of \$28,500.00 secured hereunder, including accrued interest.

4th: To the payment of the amount due and unpaid on any additional sums borrowed or advanced under and in accordance with the provisions of this Declaration of Trust, and secured thereby, together with accrued interest thereon.

5th: AND the balance (if any) to the person or persons legally entitled thereto.

AND, in the event of such sale of the beneficial interest hereunder or any portion or portions thereof, and the execution of an Assignment or Assignments thereof, under this Trust, then the recitals in each such Assignment of default and of publication of notice of sale and of demand that such sale be made, postponement of sale, terms of sale, sale, purchaser, payment of purchase money, and of any other fact or facts affecting the regularity or validity of such sale, shall be conclusive proof of such failure to pay, of due publication of such notice, and that the sale was made after due and proper demand, and of all facts recited therein; and any such Assignment containing such recitals shall be effectual and conclusive against all beneficiaries and all other persons as to such failure to pay, publication and demand, and as to all facts recited therein, and the receipt for the purchase money contained in each Assignment executed to a purchaser or purchasers as aforesaid shall be a sufficient discharge to such purchaser or purchasers from all obligation to see to the proper application of the purchase money.

AND THE BENEFICIARY HEREUNDER, by his approval of this Declaration and for himself and his heirs and assigns, does transfer, assign and convey to said Trustee title to the entire beneficial interest under this Trust sufficient to enable said Trustee to transfer, assign and convey said interest, or part or parts thereof, upon each sale thereof as hereinbefore in this section provided.

In the event of a default and conveyance and sale of the Trust property, as in this Article provided, or in the event of the merger of the interests of the Beneficiary, and the payee hereunder by assignment or otherwise, or when all the terms of this Trust shall have been complied with by the Beneficiary and the Payee hereunder, it is understood and agreed between all parties hereto that the title to any property covered by any then existing agreement of sale executed by the Trustee shall remain in the name of the Trustee for the benefit of the real owner thereof, and the proceeds received therefrom shall be applied, as in Article Fourth provided, to the payment of any unpaid commissions due the Agent, and to the costs, fees and expenses of [85] the Trustee; and the Balance of the proceeds to be paid to the then real owner of said property.

In the event of the full payment of any Agreement by the purchaser therein named, or his successors in interest, the Trustee shall thereupon convey the property covered by said agreement to such purchaser, in accordance with the terms of said agreement.

ARTICLE SEVENTEENTH: If the funds in the hands of said Trustee belonging to this Trust are not sufficient to pay, when due, the principal or interest of any mortgage or deed of trust or other debt, pledge or incumbrance against the property covered hereby, or any taxes, insurance, assessments, liens, costs, charges or other expenses necessary or proper for the preservation, maintenance and care of said Trust Estate or the title thereto, or the costs,

charges and expenses of this Trust, then and in any such event, the Trustee is authorized to levy assessments on the Beneficiary, from time to time, to meet such charges and expenses, and each Beneficiary, his heirs, successors and assigns, does, by his approval and ratification of the terms of this Declaration of Trust, well and truly bind himself to pay to the Trustee his proper proportion thereof on or before the day upon which the same shall become due and payable.

AND in the event that any one or more of said Beneficiaries shall fail to so pay his proportionate share of any such sum or assessment on or before the day it shall become due and payable, said Trustee, or any one of the other Beneficiaries of the Trust may pay such share to the end that said Trust Estate, the trusts herein contained, and all parties interested herein, may be protected; and any such Beneficiary shall be entitled to receive seven per cent (7%) interest upon any sums so advanced, from the date of advancement until repaid.

IN THE EVENT of such default and exercise of the right above granted, the Trustee, shall, upon the written demand of any party making such payment, and after thirty (30) days demand on such defaulting Beneficiary for the repayment of such amount advanced (if such amount advanced is not repaid within thirty (30) days after such demand), sell the interest of such defaulting Beneficiary hereunder, and all his interest in and to the proceeds and avails arising or growing out of this Declaration of Trust, or so much thereof as it shall be necessary to sell

in order to pay to the party making such payment the amount so paid by him, with interest thereon at the rate of seven per cent (7%) per annum, the expenses of such sale and the compensation of the Trustee in the sum of one hundred dollars (\$100.00).

Such sale shall be made subject to all of the terms and conditions of this Trust at either public or private sale, at the option of the Trustee. [86]

If said sale shall be made at private sale, the interest of such defaulting Beneficiary shall be sold for a price of not less than the amount such defaulting Beneficiary shall have paid on account of said purchase price and the costs of such sale. Should the Trustee elect to sell such interest at public auction, then said sale shall be made in the following manner, to-wit:

Said Trustee shall first public notice of the time and place of such sale, with a brief description of the interest of such defaulting Beneficiary hereunder to be sold, at least once a week for four successive weeks in some newspaper published in the County of Los Angeles, State of California, and may, from time to time, postpone such sale by publication in the same newspaper, or, at its option, by public announcement thereof at the time and place of sale so advertised; and on the date of sale or on the date to which such sale may be postponed, said Trustee shall sell the Beneficial Interest hereunder so advertised, or any portion thereof, at public auction, at such place in the City of Los Angeles, State of California, as it may have designated, to

the highest bidder, for cash, in **LAWFUL MONEY** of the United States, and any of the Beneficiaries hereunder, or any other person, may bid and purchase at such sale, and thereafter such purchaser shall have all the rights and privileges of an original Beneficiary hereunder, subject, however, to all of the terms and conditions of this Trust.

AND said Beneficiaries do hereby, by their approval of this Trust, jointly and severally transfer and convey to said Trustee title to said Beneficial interest or interests, sufficient to enable said Trustee to convey and assign said interest or interests upon a sale thereof, in event of a default as above provided.

Upon a sale of said interest at either public or private sale said Trustee shall execute and deliver to the purchaser or purchasers, his or their heirs or assigns, an assignment of the interest so sold, and out of the proceeds thereof, shall pay:

1st: The expenses of such sale and the compensation of the Trustee in the sum of One Hundred Dollars (\$100.00), in **LAWFUL MONEY** of the United States, which amount shall become due and payable upon demand made as hereinbefore provided for the sale of the interest of such defaulting Beneficiary.

2nd: To the person having paid the same, the amount paid for the account of said defaulting Beneficiary as above provided, together with interest thereon at the rate of seven per cent (7%) per annum, from the date of such default to the date of

receipt by the Trustee of proceeds from such sale; and [87]

LASTLY: The Balance or surplus of such proceeds, if any, to the order of such defaulting Beneficiary, his heirs or assigns.

IN THE EVENT of a sale of the interest of such defaulting Beneficiary, or any part thereof, at either public or private sale, and the execution of an assignment thereof under these trusts, then the recitals therein of default, and of such publication of notice of sale, and of a demand that such sale should be made, postponement of sale, terms of sale, sale, purchaser, payment of purchase money and of any other fact or facts affecting the regularity or validity of such sale, shall be conclusive proof of such default, of the due publication of such notice, that such sale was made on due and proper demand and of all the facts recited in said assignment; and such assignment, with such recitals therein, shall be effectual and conclusive against the said defaulting Beneficiary, his heirs or assigns and all other persons, as to such default, publication and demand, and as to all other facts recited therein, and the receipt for the purchase money contained in any assignment executed to a purchaser as aforesaid shall be sufficient to discharge such purchaser from all obligation to see to the proper application of the purchase money.

ARTICLE EIGHTEENTH: The interest under this Trust of each Beneficiary and the Agent hereunder is personal property and that no such Beneficiary or Agent has any right, title or interest in or

to the property covered hereby, and has no right or power to in any manner apply for or secure the dissolution or termination of this Trust, or the partition or the division of any of the Trust property: the sole right and power of each Beneficiary hereunder being to enforce the performance of the terms of this Trust, as expressly set forth in this Declaration.

PROVIDED, HOWEVER, that after the payment in full of the indebtedness secured hereby, if any, and the termination of the Agency Appointment, if any, made in accordance with the terms of this Trust, all of the Beneficiaries of this Trust, by a jointly written direction of the Trustee, may close and terminate this Trust. In no event, however, shall the Trustee be required to convey any property then covered by any existing Agreement to Convey executed by the trustee, but the Trustee is expressly empowered and directed to retain the title to the property covered by any such existing Agreement to Convey, for the benefit of the real owner thereof. The proceeds and avails received from any such Agreement to Convey shall be applied by the Trustee to the payment of any unpaid commission due, and to the costs, fees and expenses of the Trustee, and the balance of the proceeds shall be paid by the Trustee to the then real owner of such Agreement to Convey. [88]

ARTICLE NINETEENTH: The said Trustee makes no representation of fact as to the title to the property held under this Trust, but has the right to assume that the Guarantee of Title issued by any

Title Company doing business in the County in which the Trust property, or some part thereof, is situated, correctly shows the record title to said property and the incumbrances thereon.

ARTICLE TWENTIETH: The Beneficiaries may sell, transfer and assign all or any part of their beneficial interest herein provided that no sale or transfer of any beneficial interest hereunder shall be valid or binding upon said Trustee until an executed original of the assignment or other instrument evidencing such sale or transfer has been filed with said Trustee with a transfer fee of \$10.00 for each transfer, and shall by endorsement thereon be accepted by the Assignee and Trustee; excepting only where such interest may pass or be transferred by Decree or Order of Court, and then only upon satisfactory proof of the regularity and validity of the proceedings in such matter being presented to said Trustee.

ARTICLE TWENTY FIRST: This Trust shall not cease or terminate in any event until all the costs, fees and expenses of said Trustee hereunder shall have been fully paid, nor until each party to this Trust has delivered to the Trustee for cancellation, its, his or her certified copy of this Declaration of Trust, together with the Certificate of Beneficial Interest attached thereto, if any.

ARTICLE TWENTY SECOND: The term Beneficiary used herein shall include Beneficiaries; that the masculine gender shall include the feminine and neuter genders; that the singular number shall

include the plural number, all wherever and as to the context of the language herein contained shall indicate.

ARTICLE TWENTY THIRD: Said Trustors have delivered to the Trustee as additional property under this Trust, certain street improvement bonds issued by the County of Los Angeles, under the County Improvement Act of 1921, being County Improvement Number 52, Series One, as follows:

Bond No.	Amount
578	\$ 246.06
579	123.03
580	1184.29
581	592.14
582	1637.85
583	696.58

[89]

The said Trustee certifies that it has received said bonds to be held by it in trust, subject to all the conditions and terms of this Declaration of Trust, and said Trustee is authorized and empowered to, at any time, surrender said bonds for cancellation if and when in its sole judgment, it shall deem it necessary to do so, and especially when upon sale of any part of the subdivided property against which these bonds appear as a lien, it shall be required to sell or convey the property covered by such bond, free and clear of any indebtedness.

ARTICLE TWENTY FOURTH: The conditions and provisions hereof shall inure to and bind the beneficiaries as joint tenants and their assigns and also the heirs, legatees, devisees, administrators, ex-

ecutors, successors and assigns of the surviving joint tenant, and shall also inure to and bind all other parties hereto their heirs, legatees, devisees, administrators, executors, successors and assigns.

IN WITNESS WHEREOF, the said SECURITY TRUST & SAVINGS BANK has caused these presents to be executed in its corporate name by its Vice President and Assistant Secretary, thereunto duly authorized, and its corporate seal to be hereto attached as of the 15th day of July, 1925.

SECURITY TRUST & SAVINGS BANK

By J. VEENHUYZEN,

Vice President.

By E. B. PENTZ,

Ass't Secretary.

We, the undersigned, do hereby certify and declare that we are the Beneficiaries and Payee named in the above and foregoing Declaration of Trust and that the above and foregoing Declaration of Trust Number 2-1780, of the SECURITY TRUST & SAVINGS BANK, correctly and accurately sets forth and declares the trusts under and upon which said property is held by the said Trustee, and we do also hereby agree to and do approve, ratify and confirm the same in all particulars.

And the undersigned Beneficiaries and Payee, for themselves and their heirs and assigns do transfer, assign and convey [90] to said Trustee title to the Beneficial interests under said Trust for conveyance of said interest, or part or parts thereof, in event of a sale as provided in Article Sixteenth and/or Article Seventeenth of said Declaration of Trust.

DATED at Los Angeles, California, this 15th day of July, 1925.

ROBERT JAMES RICHARDS
ARABELLA GRACE RICHARDS
SECURITY TRUST & SAVINGS BANK,

Payee,

By: J. VEENHUYZEN,
Vice President.

By: E. B. PENTZ,
Assistant Secretary.

I, the undersigned, the herein appointed agent, accept such appointment subject to all the terms and conditions of this Declaration of Trust.

P. N. SNYDER,
Agent.

STATE OF ILLINOIS,
COUNTY OF COOK.—ss.

On this 15th day of July, 1925, before me, RUSSELL S. CLARK, a Notary Public in and for said County, personally appeared ROBERT JAMES RICHARDS and ARABELLA GRACE RICHARDS, husband and wife, of Los Angeles County, California, known to me to be the persons whose names are subscribed to the foregoing instrument and acknowledged that they executed the same; and I certify that under the laws of Illinois I am duly authorized to take acknowledgments of deeds.

WITNESS my hand and official seal.

RUSSELL S. CLARK,

Notary Public in and for the County of Cook,
State of Illinois.

RICHARD'S UNIT #1.

Tract #8790.

Lot	Price	Lot	Price
1	\$40,000.00	31	\$3,000.00
2	5,000.00	32	3,000.00
3	3,750.00	33	3,000.00
4	4,000.00	34	3,000.00
5	12,500.00	35	3,000.00
6	3,125.00	36	3,000.00
7	3,125.00	37	3,000.00
8	3,125.00	38	3,000.00
9	3,125.00	39	3,000.00
10	3,125.00	40	3,000.00
11	3,125.00	41	3,000.00
12	3,125.00	42	3,000.00
13	3,125.00	43	3,000.00
14	3,125.00	44	3,000.00
15	3,125.00	45	1,450.00
16	3,125.00	46	1,450.00
17	3,125.00	47	1,450.00
18	3,125.00	48	1,450.00
19	3,125.00	49	1,450.00
20	3,125.00	50	1,450.00
21	3,125.00	51	1,450.00
22	3,125.00	52	1,450.00
23	3,125.00	53	2,250.00
24	3,125.00	54	2,250.00
25	3,125.00	55	1,475.00
26	3,125.00	56	1,475.00
27	12,250.00	57	1,475.00
28	12,250.00	58	1,475.00
29	3,000.00	59	1,475.00
30	3,000.00	60	1,475.00

Lot	Price	Lot	Price
61	1,475.00	91	1,450.00
62	1,475.00	92	1,450.00
63	1,475.00	93	1,425.00
64	1,475.00	94	1,425.00
65	1,500.00	95	1,425.00
66	10,000.00	96	1,425.00
67	3,500.00	97	1,425.00
68	3,125.00	98	1,425.00
69	3,125.00	99	1,425.00
70	3,500.00	100	1,425.00
71	10,000.00	101	2,175.00
72	1,500.00	102	2,175.00
73	1,475.00	103	1,450.00
74	1,475.00	104	1,450.00
75	1,475.00	105	1,450.00
76	1,475.00	106	1,450.00
77	1,475.00	107	1,450.00
78	1,475.00	108	1,450.00
79	1,475.00	109	1,450.00
80	1,475.00	110	1,450.00
81	1,475.00	111	1,450.00
82	1,475.00	112	1,450.00
83	2,250.00	113	1,475.00
84	2,250.00	114	10,000.00
85	1,450.00	115	3,125.00
86	1,450.00	116	3,125.00
87	1,450.00	117	3,125.00
88	1,450.00	118	3,125.00
89	1,450.00	119	3,125.00
90	1,450.00	120	3,125.00

Lot	Price	Lot	Price
121	3,125.00	150	1,550.00
122	3,125.00	151	1,425.00
123	3,125.00	152	1,425.00
124	3,125.00	153	1,425.00
125	3,125.00	154	2,650.00
126	3,125.00	155	1,800.00
127	3,125.00	156	1,425.00
128	3,125.00	157	1,425.00
129	3,125.00	158	1,425.00
	[92]	159	1,275.00
130	7,500.00	160	4,250.00
131	3,750.00	161	3,750.00
132	4,250.00	162	3,750.00
133	1,250.00	163	4,250.00
134	1,450.00	164	1,550.00
135	1,450.00	165	1,400.00
136	1,450.00	166	1,400.00
137	1,450.00	167	2,400.00
138	1,450.00	168	1,800.00
139	1,900.00	169	1,400.00
140	1,900.00	170	1,400.00
141	1,450.00	171	1,250.00
142	1,450.00	172	4,250.00
143	1,450.00	173	3,750.00
144	1,450.00	174	3,750.00
145	1,500.00	175	4,250.00
146	4,250.00	176	1,500.00
147	3,750.00	177	1,400.00
148	3,750.00	178	2,250.00
149	4,250.00	179	2,350.00

Lot	Price	Lot	Price
180	1,650.00	185	3,750.00
181	1,600.00	186	4,250.00
182	1,600.00		<hr/>
183	3,750.00		\$529,300.00
184	3,750.00		

SCHEDULE OF MINIMUM SALES PRICES

Approved:

ROBERT JAMES RICHARDS

ARABELLA GRACE RICHARDS

A photostatic copy of Petitioner's Exhibit "E" is as follows: [93]

Petitioner's Exhibit "F", attached to the foregoing affidavit, is in the words and figures as follows:

DECLARATION OF TRUST.

Trust No. 2-1850.

KNOW ALL MEN BY THESE PRESENTS:

That SECURITY TRUST & SAVINGS BANK, a corporation organized under the laws of the State of California, with its principal place of business at Los Angeles, California, hereinafter sometimes called the "TRUSTEE", has received from ROBERT JAMES RICHARDS and ARABELLA GRACE RICHARDS, his wife, of Los Angeles, California, hereinafter sometimes called the "TRUSTOR" and/or "BENEFICIARIES", a deeds dated July 15th, 1925 and July 29th, 1926, as filed for record August August 21st, 1925 and July 31, 1926, conveying to it that certain real prop-

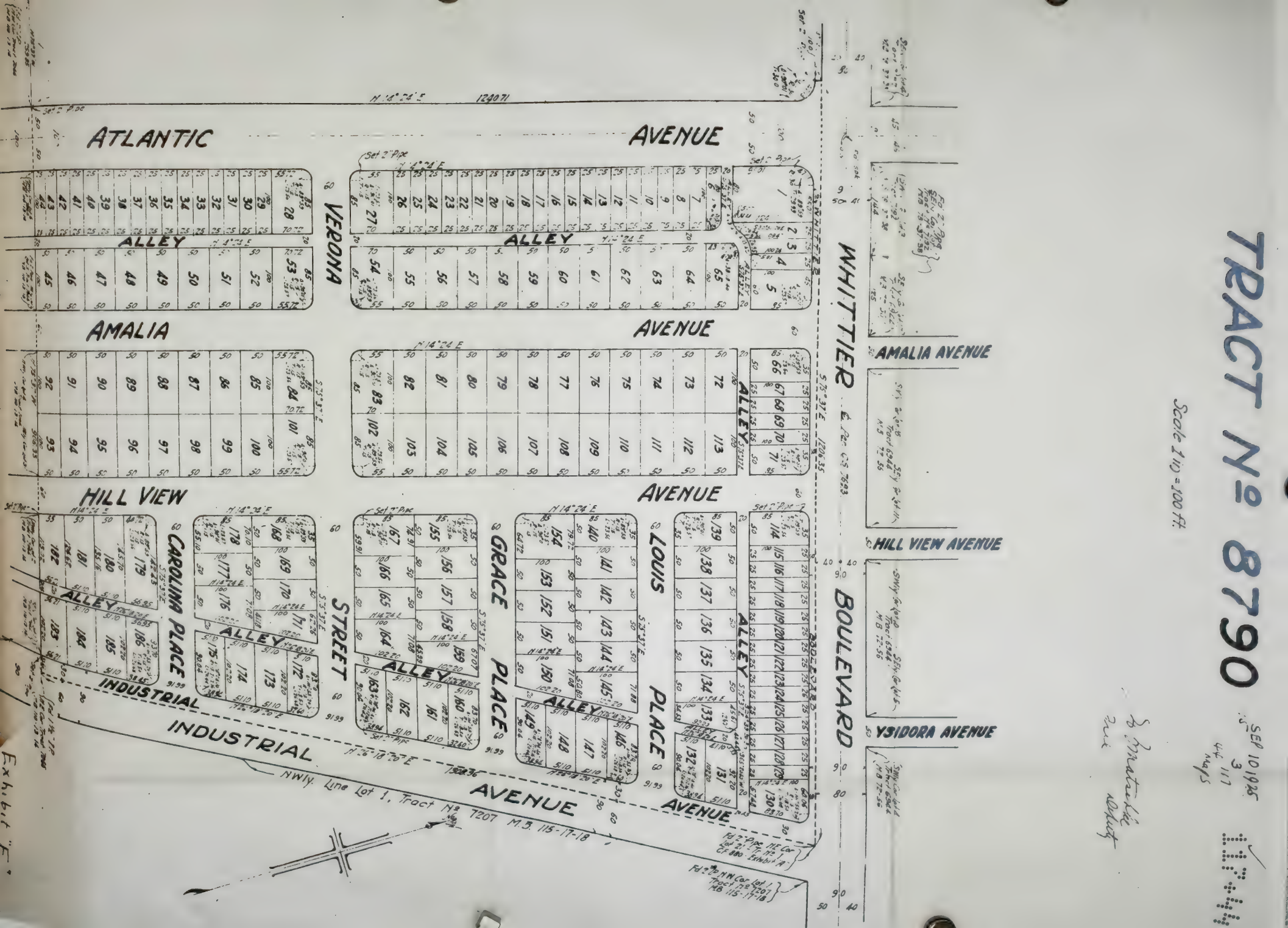
TRACT N^o 8790

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erty situated in the County of Los Angeles, State of California, as follows:

PARCEL 1: That portion of Lot Twenty (20) of the Rancho Laguna, in the County of Los Angeles, State of California, as per map attached to the final decree of partition in Case No. B25296, Superior Court of said County, and recorded in Book 6387, Page 1 et seq., of Deeds, in the office of the County Recorder and described as follows:

Beginning at a point in the Southerly line of the Whittier Road distant North seventy-five degrees (75°) Thirty-seven minutes ($37'$) West, six hundred sixty-four and forty-nine hundredths (664.49) feet from the North East corner of said Lot Twenty (20); thence South fourteen degrees (14°) twenty-three minutes ($23'$) West, twelve hundred eighty (1280) feet to a point in the southerly line of said lot distant North seventy-five degrees (75°) thirty-seven minutes ($37'$) West, six hundred sixty-four and forty-nine hundredths (664.49) feet from the South East corner of said Lot Twenty (20); thence along the Southerly line of said lot, north seventy-five degrees (75°) thirty-seven minutes ($37'$) West, one hundred thirty-eight and six hundredths (138.06) feet to the South East corner of the land conveyed by R. W. Poindexter and wife, to Samuel Pawder and Mary Maud Pawder, by deed filed for [95] record March 28th, 1921; thence North fourteen degrees (14°) twenty-three minutes ($23'$) East along the East line of land so conveyed,

twelve hundred eighty (1280) feet to the southerly line of the Whittier Road; thence along said southerly line South seventy-five degrees (75°) thirty-seven minutes ($37'$) East, one hundred thirty-eight and six hundredths (138.06) feet to the point of beginning.

PARCEL 2: That portion of lot Twenty-three (23) of the Rancho Laguna, in the County of Los Angeles, State of California, as per map attached to the certified copy of the final decree of partition, in Case No. B-25296, of the Superior Court of said County, recorded in Book 6387 Page 1 et seq., of Deeds, Records of said County, described as follows:

Beginning at an iron pipe set in the Northerly line of said Lot Twenty-three (23) at a point distant North seventy-five degrees (75°) thirty-seven minutes ($37'$) West, four hundred ninety-eight and eighty-five hundredths (498.85) feet from the most Easterly corner of said Lot; thence South fourteen degrees (14°) twenty-three minutes ($23'$) West, twenty hundred forty-four and sixty-nine hundredths (2044.69) feet to an iron pipe set in the North Easterly line of the Anaheim Telegraph Road at a point distant South sixty-one degrees (61°) twenty minutes ($20'$) forty-five seconds ($45''$) East, eight hundred forty-seven and thirty hundredths (847.30) feet from the most Westerly corner of said Lot; thence along the North Easterly line of said Road, North sixty-one degrees (61°) twenty minutes ($20'$) forty-five seconds ($45''$) West,

eight hundred forty-seven and thirty hundredths (847.30) feet to an iron pipe at the most Westerly corner of said Lot Twenty-three (23); thence North fourteen degrees (14°) twenty-three minutes (23') East, eighteen hundred thirty-five and eighty-three hundredths (1835.83) feet to an iron pipe set at the most Northerly corner of said Lot; thence along the dividing line between Lots Twenty (20) and Twenty-three (23) of said Rancho Laguna, South seventy-five degrees (75°) thirty-seven minutes (37') East, eight hundred twenty-one and fifteen hundredths (821.15) feet to the point of beginning; and being marked on said map "John F. Coutts". [96] and as shown by Guarantees No. 607622 and 668355 of the Title Guarantee and Trust Company, dated August 21, 1935 and August 9, 1926, the title to said property vested in the SECURITY TRUST & SAVINGS BANK, a corporation, free of encumbrances, except

(1) Taxes for the fiscal year 1926-27.

That no consideration was paid by said Trustee for the conveyance to it of said real property, but the consideration therefor was heretofore paid by Robert James Richards and Arabella Grace Richards, his wife, and the same was received by said Trustee herein, IN TRUST, with power of sale, for the purpose of subdividing, renting, leasing, selling and conveying said property in accordance with the terms and conditions hereinafter set forth.

ARTICLE FIRST: During the continuance of these trust the Beneficiaries agree as follows:

(a) To pay before delinquency all taxes and assessments levied and assessed against and upon the property covered hereby.

(b) To pay, when due, all other claims, liens and encumbrances affecting, or purporting to affect the title to the property covered hereby, and all costs, charges, interest and penalties on account thereof; and also all costs, fees, charges and expenses of the Trustee and of these Trusts.

(c) To appear in and defend or cause to be defended any action or proceeding at law affecting, or purporting to affect, the property covered hereby, these trusts, or the rights of the Trustee hereunder; and the said Beneficiaries hereby agree to pay all costs and expenses of any such action or proceeding, together with attorneys fees in a reasonable sum to be fixed by the Court whether any such action or proceeding progress to judgment or not, and whether brought by or against the Trustee hereunder.

(d) To protect, preserve and defend said property and the title thereto, and to keep said property in good condition, by proper care, inspection, repair, cultivation, irrigation, fertilization or otherwise, and to permit no waste or deterioration thereof, and also to pay for all improvements contracted for or ordered by the said Beneficiaries or their agent.

(e) To file with the Trustee a copy of each contract let for any improvements to be placed on each unit of the trust property as subdivided, and any such improvements placed upon the trusts prop-

erty will be superintended by the Agent, hereinafter appointed. [97]

(f) In the event the Beneficiaries shall fail to put in and pay for the improvements promised and guaranteed by them or their agents to the purchasers of lots or parcels of property in this Trust, the Trustee shall have the authority, and is hereby given express authority, to contract for and to have installed upon the property all or any of said improvements so promised and guaranteed by the Beneficiaries, and for the purpose of paying for said improvements, is hereby given the further authority and right to impound sufficient funds out of the moneys coming to it under this Trust belonging to the Beneficiaries to pay for the said improvements so contracted, either by the Beneficiaries or by the Trustee on behalf of said Beneficiaries.

The Beneficiaries agree to file with the Trustee specifications covering the improvements so promised by them or their agents and should the Beneficiaries fail so to do, the Trustee is hereby given the authority to contract and pay for improvements, which in its sole discretion, shall appear to said Trustee to meet the promises of the Beneficiaries or their agents as set forth either in the printed matter of the Beneficiaries or their agents or from evidence presented to the Trustee by purchasers of said trust property.

(g) The Trustee shall not be required to issue any deed or contract until said Beneficiaries have

filed with the Trustee a copy of each such contract as called for in paragraph (e) herein.

(h) The said Beneficiaries agree to file with the Trustee a copy of all of the advertising and printed matter used by them or their agents in connection with the sale of the trust property and also a form of the receipt given to the purchasers for any moneys received by them in connection therewith; also a copy of any promises and representations made by themselves or their agents as to improvements to be placed upon the trust property, and as to any representations to their purchasers as to any re-sales to be made by them, and also which they may permit their sub-agents to make and represent to their purchasers.

(i) To repay, within thirty (30) days from the date of advancement, and without demand, all sums advanced or expended by the Trustees under the terms hereof, with interest thereon from the date of advancement until repaid, at the rate of seven per cent (7%) per annum. Should said Beneficiaries fail or refuse to make any of the payments, or do any of the acts in the manner and at the times above provided, then the Trustee, without notice to the Beneficiaries, may make or do the same in such manner and to such extent as [98] they, or either of them may select, and to that end, said Trustee may enter and take possession of said property at such time or times and for such period or periods as they or either of them may deem necessary and/or proper; and said Trustee may pay, purchase,

contest or compromise any claims, liens, or incumbrances which in their judgment or the judgment of either of them appear to affect said property or these trusts, and may advance money or moneys from time to time for any payment or purpose whatsoever in connection with this trust; it being distinctly understood, however, that the Trustee shall be under no obligation to do any of the things mentioned above.

Upon failure of the Beneficiaries to repay to the Trustee any sums advanced by them as herein provided for, together with interest thereon at the time and in the manner as herein specified such act shall constitute a default hereunder and subject the Beneficiaries to a sale of their rights hereunder as provided in Article.....herein.

ARTICLE SECOND: The real property covered hereby is to be subdivided and the same shall be improved by the Beneficiaries hereunder in such manner as shall be agreed upon by said Trustee and said Beneficiaries.

ALL COSTS AND EXPENSES, however, incident to such subdivision and improvements shall be borne solely by said Beneficiaries, and no part thereof shall be borne by said Trustee.

AND said Beneficiaries, by their approval of this Declaration, also do promise and agree to protect and save harmless said Trustee hereunder from all loss, damage, liability and expense, by reason of such subdivision and improvements of the Trust property and likewise do promise and agree to fur-

nish to the Trustee, prior to incurring any obligations in connection with such subdivision and improvements, bond or bonds in substance and in form approved by the Trustee, protecting and indemnifying the Trustee from all loss, damage, liability and expense, by reason of the subdivision and improvements of the trust property.

ARTICLE THIRD: The Trustee shall rent, lease, sell or convey said property or any portions thereof and/or the lots or any part of any lot or lots in any subdivision thereof to such person or persons and at such prices and upon such terms and conditions as said Trustee shall deem advisable. **PROVIDED** that the sales prices of said lots or parts of any lot or lots shall not be less than those indicated on the Schedule of Minimum Sales Prices hereafter to be agreed upon by said Trustee and the Beneficiaries hereunder, a copy of which sales prices shall be attached hereto and shall be a part hereof. [99]

It is mutually understood and agreed between the Trustor, Trustee and Agent, hereinafter appointed, that the sales prices of any unsold lot or parts of any unsold lot or lots shall be increased two per cent (2%) ninety days after the date of the execution of this Trust Agreement, and a two per cent (2%) increase shall be made on all unsold lots or parts thereof every sixty days thereafter.

ARTICLE FOURTH. All proceeds received by said Trustee, arising from each sale made hereunder or from the rents, leases, and sales of said

property, shall be disbursed and distributed as follows:

1. As to sales made for cash, the Trustee shall credit:

(a) to a "Commission Fund" twenty-two and one-half ($22\frac{1}{2}\%$) per cent of the sales price of each lot or part thereof so sold as commission due the Agent hereunder.

(b) The balance to the "General Fund".

2. As to sales made for other than all cash, the Trustee shall distribute each initial payment received by it and each payment of principal thereafter received, as follows:

(a) One-third ($\frac{1}{3}$) thereof to the "Commission Fund" until the commissions due the Agent for such sale shall have been paid in full.

(b) Two-thirds ($\frac{2}{3}$) to the "General Fund".

3. All interest received shall by the Trustee be distributed to the "General Fund".

4. The moneys in the "Commission Fund" shall be distributed monthly by the Trustee to the Agent hereunder.

5. Out of the money distributed to the "General Fund" the Trustee shall pay:

(a) The costs, fees and expenses and advancements (if any) with interest, hereunder of said Trustee.

(b) Either before or after delinquency, all taxes and assessments, both general and special, levied,

assessed or imposed on or against said property or payable by the purchaser thereof from the Trustee.

Should the money in the hands of the Trustee available for that purpose be insufficient to pay said taxes or [100] assessments when due, then the Beneficiaries, by their ratification of this Declaration of Trust, covenant and agree to immediately pay to the Trustee any deficiency in the amount due on said taxes and assessments.

(c) All bills for labor incurred and materials furnished for the improvement of said property, upon the approval thereof by the Beneficiaries or Leeds & Barnard, as their engineers, or any other person designated by them.

(d) Interest on unpaid commissions of the Agent as hereinafter provided.

(e) And the remainder thereof not otherwise required for the purposes of this Trust to the said Robert James Richards and Arabella Grace Richards as joint tenants, Beneficiaries hereunder, upon the death of either, payments to be made to the survivor.

ARTICLE FIFTH: The Trustee at the request of the Beneficiaries hereunder appoints P. N. Snyder, of Los Angeles, California, as their exclusive agent to subdivide and improve and to solicit and obtain purchasers for such part of said property of which a subdivision map shall have been filed and designated herein as Unit No. 1 and to generally assume the care and custody thereof.

ALL SALES to be made by said agent shall be for prices not less than those indicated on the "Minimum Sales Price List" to be attached hereto and upon the following minimum terms:

20% of the actual sales price in cash at the date of sale, and the balance in monthly installments in an amount equal to not less than 2% of the actual sales price on all business lots, and 25% of the actual sales price in cash at the date of sale and the balance in monthly installments in an amount not less than 2% of the actual sales price on all residence lots, and interest on the unpaid balance in both cases at the rate of seven per cent per annum, payable quarterly.

A discount of 5% may be allowed if the purchase price is made in one cash payment, or a discount of 5% on the cash payment if said cash payment is in excess of 60% of the sales price of said lot or lots, or a discount of 5% may be allowed on the balance due on the purchase price of any lot or lots if such balance due is more than 60% of the purchase price which is paid in one cash payment, and a 5% building discount may be allowed to any cash purchaser of a lot at such time that a building thereon shall have been completed within one hundred and twenty (120) days from the date of executing the deed to said property and said building has been completed in its entirety with the exception of the interior finish. [101]

The Beneficiaries hereby reserve that portion of said property to be known in the new subdivision as

Lots 4, 40, 41 and 42, which lots the Trustee agrees to convey to said Beneficiaries as soon as said map is recorded.

AND each sale shall be subject to such conditions, restrictions and/or reservations and covenants as the said Trustee shall deem advisable.

The Trustee shall sell under the terms of this Trust the North one-half ($\frac{1}{2}$) and/or the South one-half ($\frac{1}{2}$) of any lot facing on Atlantic Boulevard, or the East one-half ($\frac{1}{2}$) and/or the West one-half ($\frac{1}{2}$) of any lot fronting on Mines Avenue, as per the Schedule of Sales Prices attached hereto and under the terms and conditions of this Trust, and the Trustee will issue separate deeds or contracts covering such portions.

No sale shall be made with any express or implied warranty or promise as to improvements to be made except as those specifically agreed upon by the Trustee.

This agency appointment shall be for a period of eight (8) months from the date hereof, but if the aggregate value of the lots sold in said subdivision either in cash or under contracts of sale issued by the Trustee hereunder before the expiration of said term of eight months shall equal one-half of the total aggregate value of all the lots in said subdivision as shown by the Minimum Schedule of Selling Prices to be hereto attached and herein referred to, then the Agent may, at his option, by written notice to the Trustee and Beneficiaries prior to the expiration of said term of eight months ex-

tend the term of his appointment for a further period of eight months.

In the event of the cancellation or revocation of this appointment the Trustee shall appoint such Agent or Agents as the Beneficiaries may direct, or may rent, sell, lease or convey said property to such person or persons and upon such terms as the Beneficiaries hereunder may direct. All sales of said property, however, shall be subject to the approval of the Trustee.

The said Agent shall assume the general care and custody of the subdivided unit, including the supervision of all the improvements to be placed upon the Trust property, which said improvements shall include the installation of gas, water and electricity.

The said Agent is to be paid a commission of $22\frac{1}{2}\%$ of the net sales price of each lot (which shall be the gross [102] price less all discounts allowed and not including any interest thereon), and said commission shall be paid in the manner and at the times as in this Trust Agreement provided.

In addition thereto, said Agent shall receive interest at the rate of 7% per annum on respective unpaid commissions from the date that respective purchasers have begun to pay interest until said unpaid commissions are fully paid or said sale cancelled.

The Agent shall pay out of his commissions for the advertising of the Trust property, selling expenses and his sub-agents' commissions.

The sale of each lot or portion of any lot shall be considered separately, and the receipts from that sale will be used to pay commissions solely upon said sale.

It is understood and agreed that the Trustee hereunder shall not be liable to the Beneficiaries nor to any other person for any default, defalcation or wrong-doing of the said Agent or its sub-agents.

For any service rendered by said Agent under this appointment, it shall be entitled only to such commissions as are herein set forth, and in any event, it shall be entitled only to the payment to it of the proportionate amount of the moneys actually paid in by any purchaser under any agreement of sale, or other evidence of sale and purchase in accordance with the agreed upon manner of distribution, and that no charge or claim shall be made upon the SECURITY TRUST & SAVINGS BANK, Trustee, for any portion of the unpaid commissions payable from uncollected installments owing by any such purchaser; and this Trustee, at its discretion, and for any cause whatsoever, without liability to said Agent for the balance of the unpaid commission, may cancel, annul or compromise any agreement of sale theretofore executed by it upon any portion of the foregoing described lands; the right of said Agent to a commission for such sale to cease upon any such cancellation, annulment, rescission or compromise.

The said Agent agrees to make a diligent and business-like effort to sell the said property, and

agrees to advertise the same at such times and in such manner as to create a material assistance in the selling of said property, and to pay for all such advertising.

Agent agrees to hold Trustee and Beneficiaries harmless from all loss, damage or claim arising from injury to person or property and/or out of misrepresentation or alleged misrepresentation in their acts under the agency hereby created, [103] and hereby agrees to save and hold Trustee and Beneficiaries harmless from all loss, damage or claim arising out of any default, defalcation or wrongdoing of themselves or of their salesmen or sub-agents.

The Agent agrees that nothing herein contained is intended to, nor shall it be construed as conferring any authority on Agent to execute deeds or contracts to sell said property or to enter into contracts in the name of the Trustee except temporary reservation contracts, or to incur liabilities on behalf of the Trustee and Beneficiaries; and Agent expressly agrees that except as to such temporary reservation contracts, they will enter into all contracts and incur all liabilities in their own names and behalf only and not in the name or on the behalf of Trustee and Beneficiaries.

P. N. Snyder, hereinbefore appointed agent, by his acceptance of this Declaration of Trust, accepts the agency hereby created, subject to all the terms and conditions as herein set forth.

ARTICLE SIXTH: The purchaser of each lot or lots sold hereunder from July 1st, to December 31st, 1926, shall pay the second half of taxes for 1926-27.

ARTICLE SEVENTH: The Trustee shall execute all deeds and other instruments in writing, whatsoever requisite and necessary for the renting, leasing, transferring or conveying of said property or any portion thereof. Such deeds and instruments shall be subject to conditions, restrictions, reservations and rights of way of record, if any, and shall also contain conditions and restrictions as shall be directed by the said Beneficiary and agreed to by the Trustee, and shall be subject to any and all ordinances of any city in which the property is located, or by any governmental or public agency creating or dealing with zones and prescribing the classes of buildings, structures and improvements in said zones and the use thereof.

The Trustee shall be under no liability or responsibility to the Beneficiary hereunder, nor to any other person, for the validity of any condition or restriction inserted in any Agreement of Sale or Deed, nor shall the Trustee be called upon to defend any suit, proceeding or action at law or in equity, to enforce the performance of, or enjoin the breach of, any such condition, restriction or ordinance, although the Trustee may defend or prosecute such action at its election, upon the request of the said Beneficiaries, or any other person, and upon being indemnified for its costs and expenses in any such suit or suits.

ARTICLE EIGHTH: The said Trustee shall not be required to attend to or procure any insurance upon any building upon said [104] property, or to collect or disburse any rents thereof, so long as this Trust shall continue, but all such services shall be performed and the expenses thereof borne by the said Beneficiary or his representatives.

ARTICLE NINTH: During the continuance of these trusts, the Trustee is authorized to pay: taxes levied and assessed against said property; any special assessment levied against said property or any portion thereof, of which the Trustee shall receive due notice; any other liens or charges against said property necessary for the preservation or maintenance thereof, but all of the above mentioned payments shall be at the expense of the Beneficiaries hereunder, and the said Beneficiaries, by their ratification of this Declaration of Trust, covenant and agree to pay to the said Trustee sufficient moneys with which to pay the same before the same becomes delinquent.

ARTICLE TENTH: The Trustee reserves unto itself the right, and shall have the power, solely within its discretion for the benefit of the Beneficiaries hereunder, to replace, renew, or extend any debt or incumbrance upon the Trust property, or any part thereof, when the same becomes due or at any time such replacement, renewal or extension may be in the judgment of said Trustee for the best interests of this Trust or necessary to protect the Trust property; and upon such terms and upon

such conditions and by such means of security as said Trustee may deem proper, including the right and power to convey the fee title to said property or any part thereof, to such person or corporation as it shall select for the purpose of executing and delivering the necessary note, mortgage, deed of trust, or other hypothecation, to evidence and secure such debt or debts and of reconveying said property said Trustee subject thereto, and when such reconveyances shall been so made, said Trustee shall thereupon be restored to its full estate hereunder.

It being distinctly understood that any such conveyance by said Trustee, for the purposes hereinabove stated, shall in no wise be construed as a suspension or termination of this Trust or as in any way impairing, changing or limiting the powers of the said Trustee, as herein expressed and intended. But the powers conferred in this Article shall not be exercised by the Trustee unless the Mortgagees and the Payee hereunder shall have been paid, except with their written consent.

ARTICLE ELEVENTH: The Trustee shall not be obligated to convey to the said Beneficiaries, nor to any other person, any land covered by any existing Agreement of Sale, so long as such Agreement is in force and effect, but shall be and is hereby [105] authorized to retain the title to all of said land covered by such Agreement until said Agreement has been paid in full by the holder thereof, and the land shall then be deeded to the holder of said Agreement in accordance with the

terms thereof, nor shall the trustee be obligated to convey, upon the order of the Beneficiaries hereunder, or upon the order of any party to this Trust, any property upon which an Agreement to Convey has been cancelled, until time as a cancellation thereof has been affected in form satisfactory to the said Trustee.

It is understood and agreed, however, that the Trustee, upon being indemnified by the Beneficiaries for its costs, fees, and expenses, shall upon request of the said Beneficiaries, take such legal action as may be necessary for the enforcement of the terms of any of the Agreements then outstanding and in default or take such legal action as may be necessary to obtain a Court decree quieting its title or obtain such other acquittance as is satisfactory to the Trustee, to any portion of the Trust property upon which an Agreement to Convey has been, or is to be, forfeited provided that the purchaser's unrecorded copy of such Agreement has not been surrendered to the Trustee for cancellation, but all at the cost and expense of the said Beneficiaries.

ARTICLE TWELFTH: The costs, fees and expenses of the Trustee hereunder are hereby fixed as follows:

First: For accepting this Trust and executing this Declaration a sum of one-tenth of one per cent ($\frac{1}{10}$ of 1%) of the gross selling price of said property.

Second: One per cent (1%) of the gross sales price of any sale where the sales price shall be paid in one cash payment.

Third: Two and one-half per cent ($2\frac{1}{2}\%$) of the gross sales price of any sale, including interest thereon, and where the sales price is \$6,000.00 or more and paid in deferred payments.

Fourth: Three per cent (3%) of the gross sales price of any sale, including interest thereon, and where the sales price is less than \$6,000.00 and paid in deferred payments. Three per cent (3%) on all other sums collected under the provisions of this Trust Agreement. [106]

PROVIDED, HOWEVER, that the aggregate compensation under items Second, Third and Fourth shall not be less than Two Hundred Fifty (\$250.00) Dollars per year.

Fifth: Two and 50/100 (\$2.50) Dollars per lot or part of lot for each contract in duplicate and/or mortgage and/or trust deed, and two and 50/100 (\$2.50) Dollars per lot or any part of lot for each deed executed by said Trustee.

Sixth: The necessary cost of guarantees of title, recording charges, escrow charges, the cost of printing forms of deeds, and any other charges or expenses necessary to consummate the sales of the property.

Seventh: A reasonable compensation for any service rendered by said Trustee in the execution of this Trust for which the costs, fees and expenses are not herein provided, and including a reasonable compensation (in addition to the counsel fees and other expenses) for any service rendered under this Trust by the said Trustee in connection with

any action or proceeding at law, or in paying or attending to the payment of any taxes or assessments in connection with any income tax, inheritance tax or estate tax matter affecting the Trustee any Beneficiaries hereunder, or the Trust property or any portion thereof.

ARTICLE THIRTEENTH: The said Beneficiaries, by their ratification of this Declaration of Trust, covenant and agree to hold and save harmless the Trustee hereunder from any and all liability, claims, demands, injuries or damages which it may suffer or sustain by reason of the acceptance of this Trust and its position as Trustee hereunder, and to protect said Trustee from any loss, damage, cost or expense by reason of the improvements of any character whatsoever made on said property, and against all expenses incurred by any Agent of the Beneficiaries or any Agent appointed by the trustee at the request of the Beneficiaries in the handling or sale of said property, and, upon demand of the Trustee, to furnish said Trustee with such further guaranty or indemnity as said Trustee shall deem necessary to protect said Trustee and said lands against any loss, damage, cost or expense by reason of such sale or improvements.

ARTICLE FOURTEENTH: If the whole or any portion of the interest of the Beneficiaries hereunder, or any Beneficiary, if [107] there be more than one Beneficiary, or the proceeds or avails of any such interest, shall, at any time during the terms or upon the expiration of this Trust, become liable for payment of any estate, inheritance, in-

come or other tax, charge or assessment which said Trustee shall be required to pay, then unless such taxes shall have been fully paid when due, by someone else, said Trustee is hereby authorized, without previous notice to or demand upon any person, to pay such taxes out of the whole or any portion of the interest so affected, and for that purpose is hereby generally and specifically authorized and empowered, without previous notice or demand to or from any person whomsoever, to sell, at public or private sale, and convey sufficient portion of such interest up to the whole thereof as shall fully pay all such taxes, all costs and expenses of such sale, all the sums, together with interest thereon at seven per cent (7%) per annum, payable quarterly, then due the Trustee under this Trust or which it may have advanced or expended in the care, management and protection of the Trust Estate, and in the payment of any said estate, inheritance, income or other taxes therein, and which said Trustee may be required to pay. Until such sums have been fully paid, they shall constitute a first lien on all the property subject to this tax, and in favor of said Trustee.

ARTICLE FIFTEENTH: If the funds in the hands of said Trustee belonging to this Trust are not sufficient to pay, when due, the principal or interest of any mortgage or deed of Trust, or other debt, pledge or incumbrance against the property covered hereby, or any taxes, insurance, assessments, liens, costs, charges or other expenses necessary or proper for the preservation, maintenance and

care of said Trust Estate or the title thereto, or the costs, charges and expenses of this Trust, then and in any such event, the Trustee is authorized to levy assessments on the Beneficiaries, from time to time, to meet such charges and expenses, and said Beneficiaries, their heirs, successors and assigns, do by their approval and ratification of the terms of this Declaration of Trust, well and truly bind themselves to pay to the Trustee their proper proportion thereof on or before the day upon which the same shall become due and payable.

AND in the event that any one or more of said Beneficiaries shall fail to so pay his proportionate share of any such sum or assessment on or before the day it shall become due and payable, said Trustee, or any one of the other Beneficiaries of the Trust may pay such share to the end that said Trust Estate, the trusts herein contained, and all parties interested herein, may be protected; and any such Beneficiary shall be entitled to receive seven per cent (7%) interest upon any sums so advanced, from the date of advancement until repaid.

IN THE EVENT of such default and exercise of the right [108] above granted, the Trustee shall, upon the written demand of any party making such payment, and after thirty (30) days demand on such defaulting Beneficiary for the repayment of such amount advanced (if such amount advanced is not repaid within thirty (30) days after such demand), sell the interest of such defaulting Beneficiary hereunder, and all his interest in and to the proceeds and avails arising or growing out of this

Declaration of Trust, or so much thereof as it shall be necessary to sell in order to pay to the party making such payment the amount so paid by him, with interest thereon at the rate of seven per cent (7%) per annum, the expenses of such sale and the compensation of the Trustee in the sum of One Hundred (\$100.00) Dollars.

Such sale shall be made subject to all of the terms and conditions of this Trust at either public or private sale, at the option of the Trustee.

If said sale shall be made at private sale, the interest of such defaulting Beneficiary shall be sold for a price of not less than the amount such defaulting Beneficiary shall have paid on account of said purchase price and the costs of such sale. Should the Trustee elect to sell such interest at public auction, then said sale shall be made in the following manner, to-wit:

Said trustee shall first publish notice of the time and place of such sale, with a brief description of the interest of such defaulting Beneficiary hereunder to be sold, at least once a week for four successive weeks in some newspaper published in the County of Los Angeles, State of California, and may, from time to time, postpone such sale by publication in the same newspaper, or, at its option by public announcement thereof at the time and place of sale so advertised; and on the date of sale, or on the date to which such sale may be postponed, said Trustee shall sell the Beneficial Interest hereunder so advertised, or any portion thereof, at public auction, at such place in the City of Los Angeles,

State of California, as it may have designated to the highest bidder, for cash, in LAWFUL MONEY of the United States, and any of the Beneficiaries hereunder, or any other person, may bid and purchase at such sale, and thereafter such purchaser shall have all of the rights and privileges of an original Beneficiary hereunder, subject, however, to all of the terms and conditions of this Trust.

AND said Beneficiaries do hereby, by their approval of this Trust, jointly and severally transfer and convey to said Trustee title to said Beneficial Interest or Interests, sufficient to enable said Trustee to convey and assign said interest or interests upon a sale thereof, in event of a default as above provided.

Upon a sale of said interest at either public or private sale said Trustee shall execute and deliver to the purchaser or [109] purchasers, his or their heirs or assigns, an assignment of the interest so sold, and out of the proceeds thereof, shall pay:

1st. The expenses of such sale and the compensation of the Trustee in the sum of One Hundred (\$100.00) Dollars, in lawful money of the United States, which amount shall become due and payable upon any demand made as hereinbefore provided for the sale of the interest of such defaulting Beneficiary.

2nd. To the person having paid the same, the amount paid for the account of said defaulting Beneficiary as above provided, together with interest thereon at the rate of seven per cent (7%) per annum, from the date of such default to the date of

receipt by the Trustee of proceeds from such sale; and

LASTLY: The balance or surplus of such proceeds, if any, to the order of such defaulting Beneficiary, his heirs or assigns.

IN THE EVENT of a sale of the interest of such defaulting Beneficiary, or any part thereof, at either public or private sale, and the execution of an assignment thereof under these trusts, then the recitals therein of default, and of such publication of notice of sale, and of a demand that such sale should be made, postponement of sale, terms of sale, sale, purchaser, payment of purchase money and of any other fact or facts affecting the regularity or validity of such sale, shall be conclusive proof of such default, of the due publication of such notice, that such sale was made on due and proper demand and of all the facts recited in said assignment; and such assignment, with such recitals therein, shall be effectual and conclusive against the said defaulting Beneficiary, his heirs or assigns and all other persons, as to such default, publication and demand, and as to all other facts recited therein, and the receipt for the purchase money contained in any assignment executed to a purchaser as aforesaid shall be sufficient to discharge such purchaser from all obligation to see to the proper application of the purchase money.

ARTICLE SIXTEENTH: The interest under this Trust of each Beneficiary and the Agent hereunder is personal property and that no such Beneficiary or Agent has any right, title or interest in or

to the property covered hereby, and has no right or power to in any manner apply for or secure the dissolution or termination of this Trust, or the partition or the division of any of the Trust property; the sole right and power of such Beneficiary hereunder being to enforce the performance of the terms of this Trust, as expressly set forth in this Declaration.

PROVIDED, HOWEVER, that after the payment in full of any indebtedness that may hereafter be secured hereby, and the termination of the Agency Appointment, if any, made in accordance with the terms of this Trust, all of the Beneficiaries of this Trust, by a jointly written direction of the Trustee, may close and terminate this Trust. In no event, however, shall the Trustee [110] be required to convey any property then covered by any existing agreement to convey executed by the Trustee, but the Trustee is expressly empowered and directed to retain the title to the property covered by any such existing Agreement to Convey, for the benefit of the real owner thereof. The proceeds and avails received from any such Agreement to Convey shall be applied by the Trustee to the payment of any unpaid commission due, and to the costs, fees and expenses of the Trustee, and the balance of the proceeds shall be paid by the Trustee to the then real owner of such Agreement to Convey.

ARTICLE SEVENTEENTH: The said Trustee makes no representation of fact as to the title to the property held under this Trust, but has the right to assume that the Guarantee of Title issued by any

Title Company doing business in the County in which the Trust property, or some part thereof, is situated, correctly shows the record title to said property and the incumbrances thereon.

ARTICLE EIGHTEENTH: The Beneficiaries may sell, transfer and assign all or any part of their beneficial interest herein, provided that no sale or transfer of any beneficial interest hereunder shall be valid or binding upon said Trustee until an executed original of the assignment or other instrument evidencing such sale or transfer has been filed with said Trustee with a transfer fee of \$10.00 for each transfer, and shall be endorsement thereon be accepted by the Assignee and Trustee; excepting only where such interest may pass or be transferred by Decree or Order of Court, and then only upon satisfactory proof of the regularity and validity of the proceedings in such matter being presented to said Trustee.

ARTICLE NINETEENTH: This Trust shall not cease or terminate in any event until all the costs, fees and expenses of said Trustee hereunder shall have been fully paid, nor until each party to this Trust has delivered to the Trustee for cancellation, its, his or her certified copy of this Declaration of Trust, together with the Certificate of Beneficial Interest attached thereto, if any.

ARTICLE TWENTIETH: The term "Beneficiary" used herein shall include Beneficiaries; that the masculine gender shall include the feminine and neuter genders; that the singular number shall include the plural number, all wherever and as the

context of the language herein contained shall indicate.

ARTICLE TWENTY-FIRST: The conditions and provisions hereof shall inure to and bind the Beneficiaries as joint tenants and their assigns and also the heirs, legatees, devisees, administrators, executors, successors and assigns of the surviving joint tenant, and shall also inure to and bind all other parties hereto, their heirs, legatees, devisees, administrators, executors, successors and assigns. [111]

IN WITNESS WHEREOF, the said SECURITY TRUST AND SAVINGS BANK has caused these presents to be executed in its corporate name by its Vice President and Assistant Secretary, thereunto duly authorized, and its corporate seal to be hereto attached as of the 6th day of August, 1926.

SECURITY TRUST & SAVINGS BANK

By M. N. AVERY,

OK [Corporate Seal]

Vice President.

E. P.

By E. B. PENTZ,

Assistant Secretary.

ROBERT JAMES RICHARDS,

ARABELLA GRACE RICHARDS,

Beneficiaries.

I, the undersigned, appointed Agent, accept such appointment subject to all the terms and conditions of this Declaration of Trust.

P. N. SNYDER,

Agent.

A photostatic copy of Petitioner's Exhibit "G" is in the words and figures as follows: [112]

Petitioner's Exhibit "H", attached to the foregoing affidavit, is in the words and figures as follows:

DECLARATION OF TRUST.

Trust No. 2-1899.

KNOW ALL MEN BY THESE PRESENTS:

That SECURITY TRUST & SAVINGS BANK, a corporation organized under the laws of the State of California, with its principal place of business at Los Angeles, California, hereinafter sometimes called the "TRUSTEE", has received from ROBERT JAMES RICHARDS and ARABELLA GRACE RICHARDS, his wife, of Los Angeles, California, hereinafter sometimes called the "TRUSTOR" and/or "BENEFICIARIES", a deed dated January 12, 1927, filed for record, conveying to it that certain real property situated in the County of Los Angeles, State of California, as follows:

That portion of Lot Twenty-three (23) of the Rancho Laguna, as shown on map marked Exhibit "A" filed in Superior Court Case No. B-25296, Records of said County, described as follows:

Beginning at the Southwesterly corner of Tract Number Seventy Hundred Sixty-six (7066), as per map recorded in Book 110, Pages 13 and 14 of Maps, Records of said County; thence Northwest-erly along the Northeasterly line of the Anaheim

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TRACT No 9436

SCALE 1 IN = 100 FT.

Sheet 2

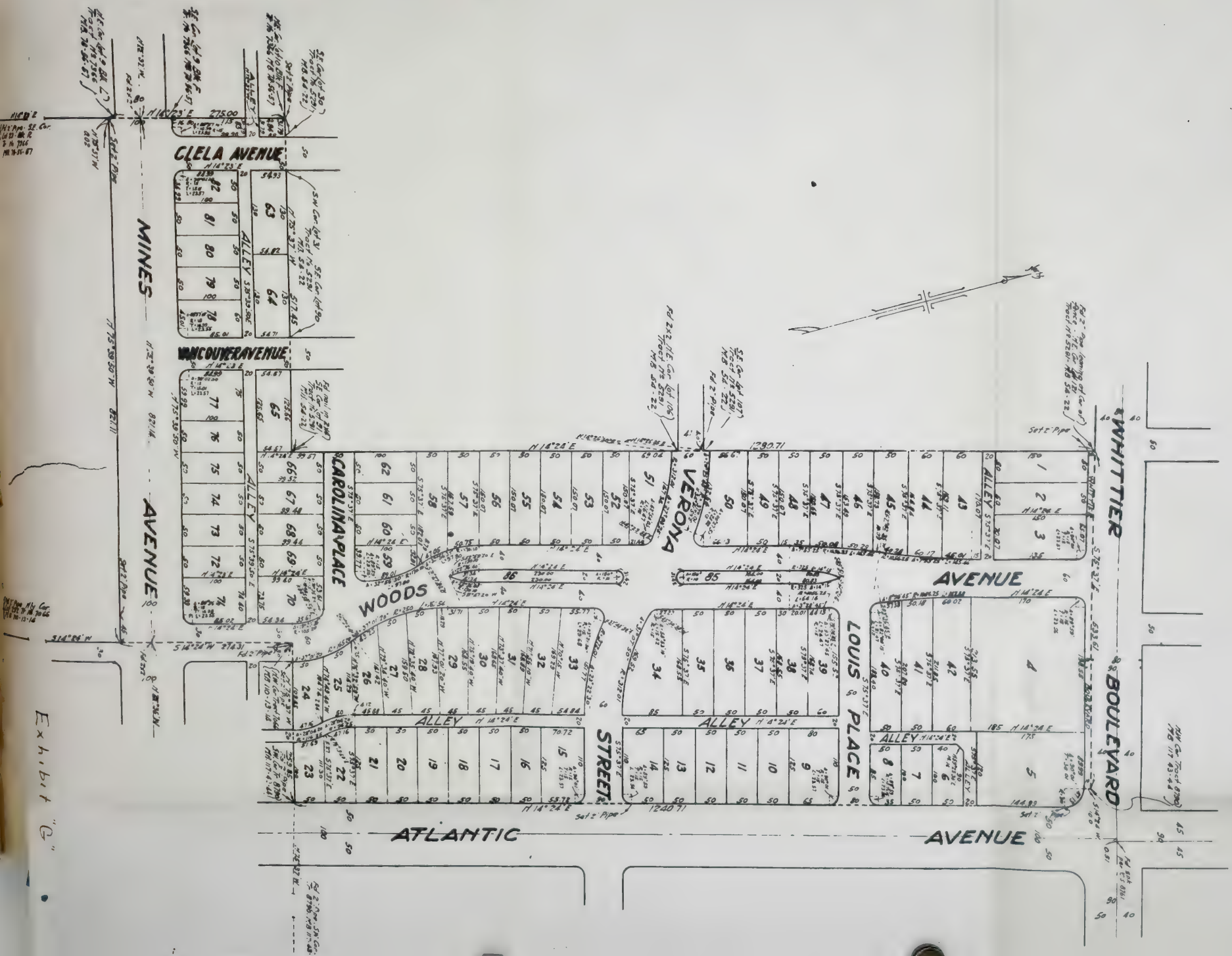


Exhibit "G"

Telegraph Road to the Southwesterly corner of said Lot Twenty-three (23); thence Northerly along the Westerly line thereof to the most Westerly corner of Tract Number Ninety-four Hundred Thirty-six (9436), as per map recorded in Book 129, Pages 8 and 9 of Maps, Records of said County; thence Easterly along the Southerly line thereof to the Westerly line of said Tract Number Seventy Hundred Sixty-six (7066); thence Southerly along said Westerly line to the point of beginning.

and as shown by Guarantee No. 699474, of the Title Guarantee and Trust Company, dated Feb. 28, 1927, the title to said property vested in the SECURITY TRUST & SAVINGS BANK, a corporation, free of incumbrances, except: [114]

(1) A right of way and perpetual easement for sewer pipe over a strip of land Eight and Sixty-six Hundredths (8.66) feet wide lying Four and Thirty-three Hundredths (4.33) feet on either side of the Westerly prolongation of a line parallel with and Four and Thirty-three Hundredths (4.33) feet, South, measured at right angles to the South line of Lot Two Hundred Ninety-Six (296), Tract Number Seventy Hundred Sixty-Six (7066) as per map recorded in Book 110, Page 13 of Maps, between the Westerly boundary of said Tract Number Seventy Hundred Sixty-Six (7066) and the Easterly boundary of Tract Number Seventy-three Hundred Sixty-six (7366) as per map recorded in Book 78, Page 56 of Maps, together with the right to enter upon and to pass and repass along said strip, etc., as granted to County Sanitation District No. 2 of

Los Angeles County, by deed dated April 7th, 1926, recorded in Book 6015, Page 44 of Official Records.

THAT no consideration was paid by said Trustee for the conveyance to it of said real property, but the consideration therefor was heretofore paid by Robert James Richards and Arabella Grace Richards, his wife, and the same was received by said Trustee herein, IN TRUST, with power of sale, for the purpose of subdividing, renting, leasing, selling and conveying said property in accordance with the terms and conditions hereinafter set forth:

ARTICLE FIRST: During the continuance of these trusts the Beneficiaries agree as follows:

(a) To pay before delinquency all taxes and assessments levied and assessed against and upon the property covered hereby.

(b) To pay, when due, all other claims, liens and encumbrances affecting, or purporting to affect the title to the property covered hereby, and all costs, charges, interest and penalties on account thereof; and also all costs, fees, charges and expenses of the Trustee and of these Trusts.

(c) To appear in and defend or cause to be defended any action or proceeding at law affecting, or purporting to affect, the property covered hereby, these trusts, or the rights of the Trustee hereunder; and the said Beneficiaries hereby agree to pay all costs and expenses of any such action or proceeding, together with attorneys fees in a reasonable sum to be fixed by the Court [115] whether any such action or proceeding progress to judgment

or not, and whether brought by or against the Trustee hereunder.

(d) To protect, preserve and defend said property and the title thereto, and to keep said property in good condition, by proper care, inspection, repair, cultivation, irrigation, fertilization or otherwise, and to permit no waste or deterioration thereof, and also to pay for all improvements contracted for or ordered by the said Beneficiaries or their agent.

(e) To file with the Trustee a copy of each contract let for any improvements to be placed on each unit of the trust property as subdivided, and any such improvements placed upon the trust property will be superintended by the Agent, hereinafter appointed.

(f) In the event the Beneficiaries shall fail to put in and pay for the improvements promised and guaranteed by them or their agents to the purchasers of lots or parcels of property in this Trust, the Trustee shall have the authority, and is hereby given express authority, to contract for and to have installed upon the property all or any of said improvements so promised and guaranteed by the Beneficiaries, and for the purposes of paying for said improvements, is hereby given the further authority and right to impound sufficient funds out of the moneys coming to it under this Trust belonging to the Beneficiaries to pay for the said improvements so contracted, either by the Beneficiaries or by the Trustee on behalf of said Beneficiaries.

The Beneficiaries agree to file with the Trustee specifications covering the improvements so promised by them or their agents and should the Beneficiaries fail so to do, the Trustee is hereby given the authority to contract and pay for improvements, which in its sole discretion, shall appear to said Trustee to meet the promises of the Beneficiaries or their agents as set forth either in the printed matter of the Beneficiaries or their agents or from evidence presented to the Trustee by purchasers of said trust property.

(g) The Trustee shall not be required to issue any deed or contract until said Beneficiaries have filed with the Trustee a copy of each such contract as called for in paragraph (e) herein.

(h) The said Beneficiaries agree to file with the Trustee a copy of all of the advertising and printed matter used by them or their agents in connection with the sale of the trust property, and also a form of the receipt given to the purchasers for any moneys received by them in connection therewith; also a copy of any promises and representations made by themselves or their agents as to improvements to be placed upon the trust property, and as to any representations to their purchasers as [116] to any re-sales to be made by them, and also which they may permit their sub-agents to make and represent to their purchasers.

(i) To repay, within thirty (30) days from the date of advancement, and without demand, all sums advanced or expended by the Trustee under the

terms hereof, with interest thereon from the date of advancement until repaid, at the rate of seven per cent (7%) per annum. Should said Beneficiaries fail or refuse to make any of the payments, or do any of the acts in the manner and at the times above provided, then the Trustee, without notice to the Beneficiaries, may make or do the same in such manner and to such extent as they, or either of them may select, and to that end, said Trustee may enter and take possession of said property at such time or times and for such period or periods as they or either of them may deem necessary and/or proper; and said Trustee may pay, purchase, contest or compromise any claims, liens or incumbrances which in their judgment or the judgment of either of them appear to affect said property or these trusts, and may advance money, or moneys from time to time, for any payment or purpose whatsoever in connection with this Trust; it being distinctly understood, however, that the Trustee shall be under no obligation to do any of the things mentioned above.

Upon failure of the Beneficiaries to repay to the Trustee any sums advanced by them as herein provided for, together with interest thereon at the time and in the manner as herein specified, such act shall constitute a default hereunder and subject the Beneficiaries to a sale of their rights hereunder as provided in Article herein.

ARTICLE SECOND: The real property covered hereby is to be subdivided and the same shall be improved by the Beneficiaries hereunder in such

manner as shall be agreed upon by said Trustee and said Beneficiaries.

ALL COSTS AND EXPENSES, however, incident to such subdivision and improvements shall be borne solely by said Beneficiaries, and no part thereof shall be borne by said Trustee.

AND said Beneficiaries, by their approval of this Declaration, also do promise and agree to protect and save harmless said Trustee hereunder from all loss, damage, liability and expense, by reason of such subdivision and improvements of the Trust property and likewise do promise and agree to furnish to the Trustee, prior to incurring any obligations in connection with such subdivision and improvements, bond or bonds in substance and in form approved by the Trustee, protecting and indemnifying the Trustee from all loss, damage, liability and expense, by reason of the subdivision and improvements of the trust property. [117]

ARTICLE THIRD: The Trustee shall rent, lease, sell or convey said property or any portions thereof and/or the lots or any part of any lot or lots in any subdivision thereof to such person or persons and at such prices and upon such terms and conditions as said Trustee shall deem advisable. PROVIDED that the sales prices of said lots or parts of any lot or lots shall not be less than those indicated on the Schedule of Minimum Sales Prices hereafter to be agreed upon by said Trustee and the Beneficiaries hereunder, a copy of which sales prices shall be attached hereto and shall be a part hereof.

ARTICLE FOURTH: All proceeds received by said Trustee, arising from each sale made hereunder or from the rents, leases and sales of said property, shall be disbursed and distributed as follows:

1. As to sales made for cash, the Trustee shall credit:

(a) to a "Commission Fund" twenty-five (25%) per cent of the sales price of each lot or part thereof so sold as commission due the Agent hereunder.

(b) The balance to the "General Fund".

2. As to sales made for other than all cash, the Trustee shall distribute each initial payment received by it and each payment of principal thereafter received, as follows:

(a) one-third ($1/3$) thereof to the "Commission Fund" until the commissions due the Agent for such sale shall have been paid in full.

(b) Two-thirds ($2/3$) to the "General Fund".

3. All interest received shall by the Trustee be distributed to the "General Fund".

4. The moneys in the "Commission Fund" shall be distributed monthly by the Trustee to the Agent hereunder.

5. Out of the money distributed to the "General Fund" the Trustee shall pay:

(a) The costs, fees and expenses and advancements (if any) with interest, hereunder of said Trustee.

(b) Either before or after delinquency, all taxes and assessments, both general and special, levied, assessed or imposed on or against said property or payable by the purchaser thereof from the Trustee.

Should the money in the hands of the Trustee [118] available for that purpose be insufficient to pay said taxes or assessments when due, then the Beneficiaries, by their ratification of this Declaration of Trust, covenant and agree to immediately pay to the Trustee any deficiency in the amount due on said taxes and assessments.

(c) All bills for labor incurred and materials furnished for the improvement of said property, upon the approval thereof by the Beneficiaries or Leeds & Barnard, as their engineers, or any other person designated by them.

(d) Interest on unpaid commissions of the Agent as hereinafter provided.

(e) And the remainder thereof not otherwise required for the purposes of this Trust to the said Robert James Richards and Arabella Grace Richards as joint tenants, Beneficiaries hereunder, upon the death of either, payments to be made to the survivor.

ARTICLE FIFTH: The Trustee at the request of the Beneficiaries hereunder appoints P. N. SNYDER, of Los Angeles, California, as their exclusive agent to subdivide and improve, and to solicit and obtain purchasers for such part of said property of which a subdivision map shall have been

filed and designated herein as Unit No. 1, and to generally assume the care and custody thereof.

ALL SALES to be made by said agent shall be for prices not less than those indicated on the "Minimum Sales Price List" to be attached hereto and upon the following minimum terms:

20% of the actual sales price in cash at the date of sale, and the balance in monthly installments in an amount equal to not less than 2% of the actual sales prices on all business lots, and 25% of the actual sales price in cash at the date of sale and the balance in monthly installments in an amount not less than 2% of the actual sales price on all residence lots, and interest on the unpaid balance in both cases at the rate of seven per cent per annum, payable quarterly.

A discount of 5% may be allowed if the purchase price is made in one cash payment, or a discount of 5% on the cash payment if said cash payment is in excess of 60% of the sales price of said lot or lots, or a discount of 5% may be allowed on the balance due on the purchase price of any lot or lots if such balance due is more than 60% of the purchase price which is paid in one cash payment, and a 5% building discount may be allowed to any cash purchaser of a lot at such time that a building thereon shall have been completed within one hundred and twenty (120) days from the date of executing the deed to said property and said building has been completed in its entirety, with the exception of the interior finish. [119]

AND each sale shall be subject to such conditions, restrictions and/or reservations and covenants as the said Trustee shall deem advisable.

No sale shall be made with any express or implied warranty or promise as to the improvements to be made except as those specifically agreed upon by the Trustee.

This Agency Appointment shall be for a period of eight (8) months from the date hereof, but if the aggregate value of the lots sold in said subdivision either in cash or under contracts of sale issued by the Trustee hereunder before the expiration of said term of eight months shall equal one-half of the total aggregate value of all of the lots in said subdivision as shown by the Minimum Schedule of Selling Prices to be hereto attached and herein referred to, then the Agent may, at his option, by written notice to the Trustee and Beneficiaries prior to the expiration of said term of eight months extend the term of his appointment for a further period of eight months.

In the event of the cancellation or revocation of this appointment the Trustee shall appoint such Agent or Agents as the Beneficiaries may direct, or may rent, sell, lease or convey said property to such person or persons and upon such terms as the Beneficiaries hereunder may direct. All sales of said property, however, shall be subject to the approval of the Trustee.

The said Agent shall assume the general care and custody of the subdivided unit, including the

supervision of all the improvements to be placed upon the Trust property, which said improvements shall include the installation of gas, water and electricity.

The said Agent is to be paid a commission of 25% of the net sales price of each lot, (which shall be the gross price less all discounts allowed and not including any interest thereon), and said commission shall be paid in the manner and at the times as in this Trust provided.

In addition thereto, said Agent shall receive interest at the rate of 7% per annum on respective unpaid commissions from the date that respective purchasers have begun to pay interest until said unpaid commissions are fully paid or said sale cancelled.

The agent shall pay out of his commissions for the advertising of the Trust property, selling expenses and his sub-agents commissions.

The sale of each lot or portion of any lot shall be considered separately, and the receipts from that sale will be used to pay commissions solely upon said sale. [120]

It is understood and agreed that the Trustee hereunder shall not be liable to the Beneficiaries nor to any other person for any default, defalcation or wrong-doing of the said Agent or its sub-agents.

For any service rendered by said Agent under this appointment, it shall be entitled only to such commissions as are herein set forth, and in any

event, it shall be entitled only to the payment to it of the proportionate amount of the moneys actually paid in by any purchaser under any agreement of sale, or other evidence of sale and purchase in accordance with the agreed upon manner of distribution, and that no charge or claim shall be made upon the SECURITY TRUST & SAVINGS BANK, Trustee, for any portion of the unpaid commissions payable from uncollected installments owing by any such purchaser; and this Trustee, at its discretion, and for any cause whatsoever, without liability to said Agent for the balance of the unpaid commission, may cancel, annul or compromise any agreement of sale theretofore executed by it upon any portion of the foregoing described lands; the right of said Agent to a commission for such sale to cease upon any such cancellation, annulment, rescission or compromise.

The said Agent agrees to make a diligent and businesslike effort to sell the said property, and agrees to advertise the same at such times and in such manner as to create a material assistance in the selling of said property, and to pay for all such advertising.

Agent agrees to hold Trustee and Beneficiaries harmless from all loss, damage or claim arising from injury to person or property and/or out of misrepresentation or alleged misrepresentation in their acts under the agency hereby created, and hereby agrees to save and hold Trustee and Beneficiaries harmless from all loss, damage or claim arising out of any

default, defalcation or wrongdoing of themselves or of their salesmen or sub-agents.

The agent agrees that nothing herein contained is intended to, nor shall it be construed as conferring any authority on Agent to execute deeds or contracts to sell said property or to enter into contracts in the name of Trustee except temporary reservation contracts, or to incur liabilities on behalf of the Trustee and Beneficiaries; and Agent expressly agrees that except as to such temporary reservation contracts, they will enter into all contracts and incur all liabilities in their own names and behalf only, and not in the name or on the behalf of Trustee and Beneficiaries.

P. N. Snyder, hereinbefore appointed agent, by his acceptance of this Declaration of Trust, accepts the agency hereby created, subject to all the terms and conditions as herein set forth.

ARTICLE SIXTH: The Trustee shall execute all deeds and [121] other instruments in writing, whatsoever requisite and necessary for the renting, leasing, transferring or conveying of said property or any portion thereof. Such deeds and instruments shall be subject to conditions, restrictions, reservations and rights of way of record, if any, and shall also contain conditions and restrictions as shall be directed by the said Beneficiary and agreed to by the Trustee, and shall be subject to any and all ordinances of any city in which the property is located, or by any governmental or public agency creating or dealing with zones and prescribing the

classes of buildings, structures and improvements in said zones and the use thereof.

The Trustee shall be under no liability or responsibility to the Beneficiary hereunder, nor to any other person, for the validity of any condition or restriction inserted in any Agreement of Sale or Deed, nor shall the Trustee be called upon to defend any suit, proceeding or action at law or in equity, to enforce the performance of, or enjoin the breach of, any such condition, restriction or ordinance, although the Trustee may defend or prosecute such action at its election, upon the request of the said Beneficiaries, or any other person, and upon being indemnified for its costs and expenses in any such suit or suits.

ARTICLE SEVENTH: The said Trustee shall not be required to attend to or procure any insurance upon any building upon said property, or to collect or disburse any rents, thereof, so long as this Trust shall continue, but all such service shall be performed and the expenses thereof borne by the said Beneficiary or his representatives.

ARTICLE EIGHTH: During the continuance of these Trusts, the Trustee is authorized to pay: taxes levied and assessed against said property; any special assessment levied against said property or any portion thereof, of which the Trustee shall receive due notice; any other liens or charges against said property necessary for the preservation or maintenance thereof, but all of the above mentioned payments shall be at the expense of the Benefi-

ciaries hereunder, and the said Beneficiaries, by their ratification of this Declaration of Trust, covenant and agree to pay to the said Trustee sufficient moneys with which to pay the same before the same becomes delinquent.

ARTICLE NINTH: The Trustee reserves unto itself the right, and shall have the power, solely within its discretion for the benefit of the Beneficiaries hereunder, to replace, renew, or extend any debt or incumbrance upon the Trust property, or any part thereof, when the same becomes due or at any time such replacement, renewal or extension may be in the judgment of said Trustee for the best interests of this Trust or necessary to protect the Trust property; and upon such terms and upon such conditions and by such means of security as said Trustee may deem proper, including the right and power to convey the fee title to said property, or any part thereof, to such person or [122] corporation as it shall select for the purpose of executing and delivering the necessary note, mortgage, deed of trust, or other hypothecation, to evidence and secure such debt or debts and of reconveying said property said Trustee subject thereto, and when such reconveyance shall have been so made, said Trustee shall thereupon be restored to its full estate hereunder.

It being distinctly understood that any such conveyance by said Trustee, for the purposes hereinabove stated, shall in no wise be construed as a suspension or termination of this Trust or as in any

way impairing, changing or limiting the powers of the said Trustee, as herein expressed and intended. But the powers conferred by this Article shall not be exercised by the Trustee unless the Mortgagees and the Payee hereunder shall have been paid in full, except with their written consent.

ARTICLE TENTH: The Trustee shall not be obligated to convey to the said Beneficiaries, nor to any other person, any land covered by any existing Agreement of Sale, so long as such Agreement is in force and effect, but shall be and is hereby authorized to retain the title to all of said land covered by such Agreement until said Agreement has been paid in full by the holder thereof, and the land shall then be deeded to the holder of said Agreement in accordance with the terms thereof, nor shall the Trustee be obligated to convey, upon the order of the Beneficiaries hereunder, or upon the order of any party to this Trust, any property upon which an Agreement to Convey has been cancelled, until time as a cancellation thereof has been effected in form satisfactory to the said Trustee.

It is understood and agreed, however, that the Trustee, upon being indemnified by the Beneficiaries for its costs, fees, and expenses, shall upon request of the said Beneficiaries, take such legal action as may be necessary for the enforcement of the terms of any of the Agreements then outstanding and in default, or take such legal action as may be necessary to obtain a Court Decree quieting its title or obtain such other acquittance as is satis-

factory to the Trustee, to any portion of the Trust property upon which an Agreement to Convey has been, or is to be, forfeited, provided that the purchaser's unrecorded copy of such Agreement has not been surrendered to the Trustee for cancellation, but all at the cost and expense of the said Beneficiaries.

ARTICLE ELEVENTH: The costs, fees and expenses of the Trustee hereunder are hereby fixed as follows:

First: For accepting this Trust and executing this Declaration a sum of one-tenth of one per cent ($1/10$ th of 1%) of the gross selling price of said property.

Second: One per cent (1%) of the gross sales price of any sale where the sales price shall be paid in one cash payment. [123]

Third: Two and one-half per cent ($2\frac{1}{2}$ %) of the gross sales price of any sale, including interest thereon, and where the Sales price is \$6,000.00 or more and paid in deferred payments.

Fourth: Three per cent (3%) of the gross sales price of any sale, including interest thereon, and where the sales price is less than \$6,000.00 and paid in deferred payments. Three per cent (3%) on all other sums collected under the provisions of this Trust Agreement.

PROVIDED, however, that the aggregate compensation under items Second, Third and Fourth shall not be less than Two Hundred Fifty (\$250.00) Dollars per year.

Fifth: Two and 50/100 (\$2.50) Dollars per lot or part of lot for each contract in duplicate and/or mortgage and/or trust deed, and Two and 50/100 (\$2.50) Dollars per lot or any part of lot for each deed executed by said Trustee.

Sixth: The necessary cost of guarantees of title, recording charges, escrow charges, the cost of printing forms of deeds, and any other charges or expenses necessary to consummate the sales of the property.

Seventh: A reasonable compensation for any service rendered by said Trustee in the execution of this Trust for which the costs, fees and expenses are not herein provided, and including a reasonable compensation (in addition to the counsel fees and other expenses) for any service rendered under this Trust by the said Trustee in connection with any action or proceeding at law, or in paying or attending to the payment of any taxes or assessments in connection with any income tax, inheritance tax or estate tax matter affecting the Trustee, any Beneficiaries hereunder, or the Trust property or any portion thereof.

ARTICLE TWELFTH: The said Beneficiaries, by their ratification of this Declaration of Trust covenant and agree to hold and save harmless the Trustee hereunder from any and all liability, claims, demands, injuries or damages which it may suffer or sustain by reason of the acceptance of this Trust and its position as Trustee hereunder, and to protect said Trustee from any loss, damage, cost or

[124] expense by reason of the improvements of any character whatsoever made on said property, and against all expenses incurred by any Agent of the Beneficiaries or any Agent appointed by the Trustee at the request of the Beneficiaries in the handling or sale of said property, and, upon demand of the Trustee, to furnish said Trustee with such further guaranty or indemnity as said Trustee shall deem necessary to protect said Trustee and said lands against any loss, damage, cost or expense by reason of such sale or improvements.

ARTICLE THIRTEENTH: If the whole or any portion of the interest of the Beneficiaries hereunder, or any Beneficiary, if there be more than one Beneficiary, or the proceeds or avails of any such interest, shall, at any time during the terms or upon the expiration of this Trust, become liable for payment of any estate, inheritance, income or other tax, charge or assessment which said Trustee shall be required to pay, then unless such taxes shall have been fully paid when due, by someone else, said Trustee is hereby authorized, without previous notice to or demand upon any person, to pay such taxes out of the whole or any portion of the interest so affected, and for that purpose is hereby generally and specifically authorized and empowered, without previous notice or demand to or from any person whomsoever, to sell, at public or private sale, and convey sufficient portion of such interest up to the whole thereof as shall fully pay all such taxes, all costs and expenses of such sale, all the sums, together with interest thereon at seven per cent.

(7%) per annum, payable quarterly, then due the Trustee under this Trust or which it may have advanced or expended in the care, management and protection of the Trust Estate and in the payment of any said estate, inheritance, income or other taxes therein, and which said Trustee may be required to pay. Until such sums have been fully paid, they shall constitute a first lien on all the property subject to this tax, and in favor of said Trustee.

ARTICLE FOURTEENTH: If the funds in the hands of said Trustee belonging to this Trust are not sufficient to pay, when due, the principal or interest of any mortgage or deed of trust, or other debt, pledge or incumbrance against the property covered hereby, or any taxes, insurance, assessments, liens, costs charges or other expenses necessary or proper for the preservation maintenance and care of said Trust Estate or the title thereto, or the costs, charges and expenses of this Trust, then and in any such event, the Trustee is authorized to levy assessments on the Beneficiaries, from time to time, to meet such chargs and expenses, and said Beneficiaries, their heirs, successors and assigns, do by their approval and ratification of the terms of this Declaration of Trust, well and truly bind themselves to pay to the Trustee their proper proportion thereof on or before the day upon which the same shall become due and payable.

AND in the event that any one or more of said Beneficiaries shall fail to so pay his proportionate share of any such sum or [125] assessment on or

before the day it shall become due and payable, said Trustee, or any one of the other Beneficiaries of the Trust may pay such share to the end that said Trust Estate, the trusts herein contained, and all parties interested herein, may be protected; and any such Beneficiary shall be entitled to receive Seven per cent (7%) interest upon any sums so advanced, from the date of advancement until repaid.

IN THE EVENT of such default and exercise of the right above granted, the Trustee shall, upon the written demand of any party making such payment, and after Thirty (30) days demand on such defaulting Beneficiary for the repayment of such amount advanced (if such amount advanced is not repaid within Thirty (30) days after such demand), sell the interest of such defaulting Beneficiary hereunder, and all his interest in and to the proceeds and avails arising or growing out of this Declaration of Trust, or so much thereof as it shall be necessary to sell in order to pay to the party making such payment the amount so paid by him, with interest thereon at the rate of seven per cent (7%) per annum, the expenses of such sale and the compensation of the Trustee in the sum of One Hundred (\$100.00) Dollars.

Such sale shall be made subject to all of the terms and conditions of this Trust at either public or private sale, at the option of the Trustee.

If said sale shall be made at private sale, the interest of such defaulting Beneficiary shall be sold for a price of not less than the amount such default-

ing Beneficiary shall have paid on account of said purchase price and the costs of such sale. Should the Trustee elect to sell such interest at public auction, then said sale shall be made in the following manner, to-wit:

Said Trustee shall first publish notice of the time and place of such sale, with a brief description of the interest of such defaulting Beneficiary hereunder to be sold, at least once a week for four successive weeks in some newspaper published in the County of Los Angeles, State of California, and may, from time to time, postpone such sale by publication in the same newspaper, or, at its option by public announcement thereof at the time and place of sale so advertised; and on the date of sale, or on the date to which such sale may be postponed, said Trustee shall sell the Beneficial interest hereunder so advertised, or any portion thereof, at public auction, at such place in the City of Los Angeles, State of California, as it may have designated, to the highest bidder, for cash, IN LAWFUL MONEY of the United States, and any of the Beneficiaries hereunder, or any other person, may bid and purchase at such sale, and thereafter such purchaser shall have all of the rights and privileges of an original Beneficiary hereunder, subject, however, to all of the terms and conditions of this Trust.

AND said Beneficiaries do hereby, by their approval of this Trust, jointly and severally transfer and convey to said Trustee title to said Beneficial Interest or Interests, sufficient to enable said Trus-

tee to convey and assign said interest or interests upon a sale thereof in event of a default as above provided. [126]

Upon a sale of said interest at either public or private sale said Trustee shall execute and deliver to the purchaser or purchasers, his or their heirs or assigns, an assignment of the interest so sold, and out of the proceeds thereof, shall pay:

1st: The expenses of such sale and the compensation of the Trustee in the sum of One Hundred (\$100.00) Dollars in LAWFUL MONEY of the United States, which amount shall become due and payable upon any demand made as hereinbefore provided for the sale of the interest of such defaulting Beneficiary.

2nd: To the person having paid the same, the amount paid for the account of said defaulting Beneficiary as above provided, together with interest thereon at the rate of seven per cent (7%) per annum, from the date of such default to the date of receipt by the Trustee of proceeds from such sale; and

LASTLY: The balance or surplus of such proceeds, if any, to the order of such defaulting Beneficiary, his heirs or assigns.

IN THE EVENT of a sale of the interest of such defaulting Beneficiary, or any part thereof, at either public or private sale, and the execution of an assignment thereof under these trusts, then the recitals therein of default, and of such publication of notice of sale, and of a demand that such sale

should be made, postponement of sale, terms of sale, sale, purchaser, payment of purchase money, and of any other fact or facts affecting the regularity or validity of such sale, shall be conclusive proof of such default, of the due publication of such notice, that such sale was made on due and proper demand of all the facts recited in said assignment; and such assignment, with such recitals therein, shall be effectual and conclusive against the said defaulting Beneficiary, his heirs or assigns and all other persons, as to such default, publication and demand, and as to all other facts recited therein, and the receipt for the purchase money contained in any assignment executed to a purchaser as aforesaid shall be sufficient to discharge such purchaser from all obligation to see to the proper application of the purchase money.

ARTICLE FIFTEENTH: The interest under this Trust of each Beneficiary and the Agent hereunder is personal property and that no such Beneficiary or Agent has any right, title or interest in or to the property covered hereby, and has no right or power to in any manner apply for or secure the dissolution or termination of this Trust, or the partition or the division of any of the Trust property; the sole right and power of such Beneficiary hereunder being to enforce the performance of the terms of this Trust, as expressly set forth in this Declaration.

PROVIDED, HOWEVER, that after the payment in full of any [127] indebtedness that may

hereafter be secured hereby, and the termination of the Agency Appointment, if any, made in accordance with the terms of this Trust, all of the Beneficiaries of this Trust, by a jointly written direction of the Trustee, may close and terminate this Trust. In no event, however, shall the Trustee be required to convey any property then covered by any existing Agreement to Convey executed by the Trustee, but the Trustee is expressly empowered and directed to retain the title to the property covered by any such existing Agreement to Convey, for the benefit of the real owner thereof. The proceeds and avails received from any such Agreement to Convey shall be applied by the Trustee to the payment of any unpaid commission due, and to the costs, fees and expenses of the Trustee, and the balance of the proceeds shall be paid by the Trustee to the then real owner of such Agreement to Convey.

ARTICLE SIXTEENTH: The said Trustee makes no representation of fact as to the title to the property held under this Trust, but has the right to assume that the Guarantee of Title issued by any Title Company doing business in the County in which the Trust property, or some part thereof, is situated, correctly shows the record title to said property and the incumbrances thereon.

ARTICLE SEVENTEENTH: The Beneficiaries may sell, transfer and assign all or any part of their beneficial interest herein, provided that no sale or transfer of any beneficial interest hereunder shall be valid or binding upon said Trustee until an exe-

cuted original of the assignment or other instrument evidencing such sale or transfer has been filed with said Trustee with a transfer fee of \$10.00 for each transfer, and shall by endorsement thereon be accepted by the Assignee and Trustee; excepting only where such interest may pass or be transferred by Decree or Order of Court, and then only upon satisfactory proof of the regularity and validity of the proceedings in such matter being presented to said Trustee.

ARTICLE EIGHTEENTH: This Trust shall not cease or terminate in any event until all the costs, fees and expenses of said Trustee hereunder shall have been fully paid, nor until each party to this Trust has delivered to the Trustee for cancellation, its, his or her certified copy of this Declaration of Trust, together with the Certificate of Beneficial Interest attached thereto, if any.

ARTICLE NINETEENTH: The term "Beneficiary" used herein shall include Beneficiaries; that the masculine gender shall include the feminine and neuter genders; that the singular number shall include that plural number, all wherever and as the context of the language herein contained shall indicate. [128]

ARTICLE TWENTIETH: The conditions and provisions hereof shall inure to and bind the Beneficiaries as joint tenants and their assigns and also the heirs, legatees, devisees, administrators, executors, successors and assigns of the surviving joint tenant, and shall also inure to and bind all other

parties hereto, their heirs, legatees, devisees, administrators, executors, successors and assigns.

IN WITNESS WHEREOF, the said SECURITY TRUST & SAVINGS BANK has caused these presents to be executed in its corporate name by its Vice-President and Assistant Secretary, thereunto duly authorized, and its corporate seal to be hereto attached as of the 12th day of January, 1927.

SECURITY TRUST & SAVINGS BANK,

By J. VEENHUYZEN,

Vice-President,

By E. B. PENTZ,

Assistant Secretary.

ROBERT JAMES RICHARDS,

ARABELLA GRACE RICHARDS,

Beneficiaries.

I, the undersigned, appointed Agent, accept such appointment subject to all the terms and conditions of this Declaration of Trust.

P. N. SNYDER, Agent.

[129]

RICHARDS' UNIT #3
TRACT #9797

January 24, 1927

Lot No.	Price	Lot No.	Price
1	6,400.00	29	1,650.00
2	8,750.00	30	1,650.00
3	8,750.00	31	1,650.00
4	8,750.00	32	1,650.00
5	8,750.00	33	1,650.00
6	8,750.00	34	1,650.00
7	10,500.00	35	2,250.00
8	15,000.00	36	2,250.00
9	8,750.00	37	1,500.00
10	8,750.00	38	1,500.00
11	8,750.00	39	1,500.00
12	8,750.00	40	1,500.00
13	8,750.00	41	1,500.00
14	14,800.00	42	1,500.00
15	1,900.00	43	1,500.00
16	1,750.00	44	1,500.00
17	1,750.00	45	1,500.00
18	1,750.00	46	1,500.00
19	1,750.00	47	1,650.00
20	1,750.00	48	5,625.00
21	2,500.00	49	6,250.00
22	2,450.00	50	10,000.00
23	1,800.00	51	12,000.00
24	1,900.00	52	6,250.00
25	2,100.00	53	6,250.00
26	1,950.00	54	6,250.00
27	1,750.00	55	12,000.00
28	1,750.00	56	1,550.00

RICHARDS' UNIT #3 (Continued)
TRACT #9797

Lot No.	Price	Lot No.	Price
57	1,600.00	86	2,250.00
58	1,600.00	87	2,250.00
59	1,600.00	88	1,700.00
60	1,600.00	89	1,700.00
61	1,600.00	90	1,700.00
62	1,600.00	91	1,700.00
63	1,675.00	92	1,700.00
64	1,675.00	93	1,650.00
65	1,675.00	94	1,650.00
66	1,675.00	95	1,650.00
67	1,675.00	96	1,650.00
68	2,250.00	97	1,650.00
69	2,250.00	98	1,650.00
70	1,750.00	99	1,600.00
71	1,750.00	100	1,500.00
72	1,750.00	101	10,000.00
73	1,750.00	102	6,250.00
74	1,750.00	103	6,250.00
75	1,750.00	104	6,250.00
76	1,875.00	105	6,250.00
77	2,750.00	106	6,150.00
78	2,750.00	107	1,600.00
79	1,875.00	108	1,700.00
80	1,775.00	109	1,900.00
81	1,775.00	110	1,800.00
82	1,775.00	111	1,750.00
83	1,775.00	112	1,300.00
84	1,775.00	113	1,200.00
85	1,775.00	114	2,100.00

RICHARDS' UNIT #3 (Continued)
TRACT #9797

Lot No.	Price	Lot No.	Price
115	1,750.00	136	1,750.00
116	1,600.00	137	1,750.00
117	1,600.00	138	1,750.00
118	1,650.00	139	1,750.00
119	1,700.00	140	1,750.00
120	1,700.00	141	1,750.00
121	1,700.00	142	2,350.00
122	1,700.00	143	2,300.00
123	2,350.00	144	1,700.00
124	2,200.00	145	1,700.00
125	1,775.00	146	1,700.00
126	1,775.00	147	1,700.00
127	1,775.00		[130]
128	1,775.00	148	1,650.00
129	1,775.00	149	1,700.00
130	1,775.00	150	1,750.00
131	1,850.00	151	1,700.00
132	2,350.00	152	1,900.00
133	1,750.00		
134	1,750.00		459,250.00
135	2,400.00		

APPROVED Jan. 28/27

R. J. RICHARDS

P. N. SNYDER

Photostatic copy of Petitioner's Exhibit "I" is as follows: [131]

Photostatic copies of Petitioner's Exhibits "J" and "K" are as follows: [133]

EB 23 1927
136
3 1/2
M. P.

Applicable
to
all

TRACT N 9797
IN THE COUNTY OF LOS ANGELES
SCALE: 1"=100'

SHEET 6 OF 6 SHEETS

Note:
See Cinct Certificate
regarding lots A, B, C & D

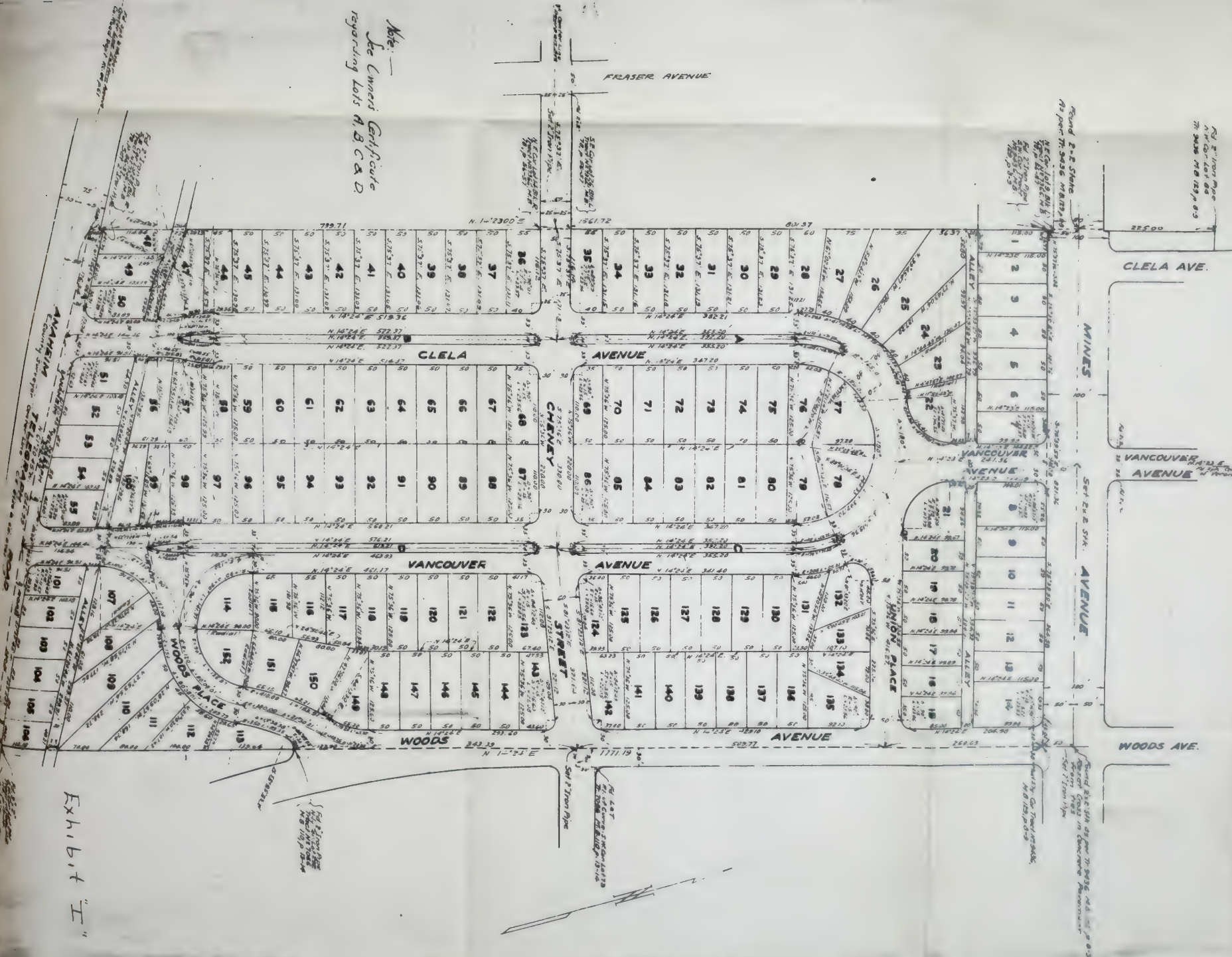


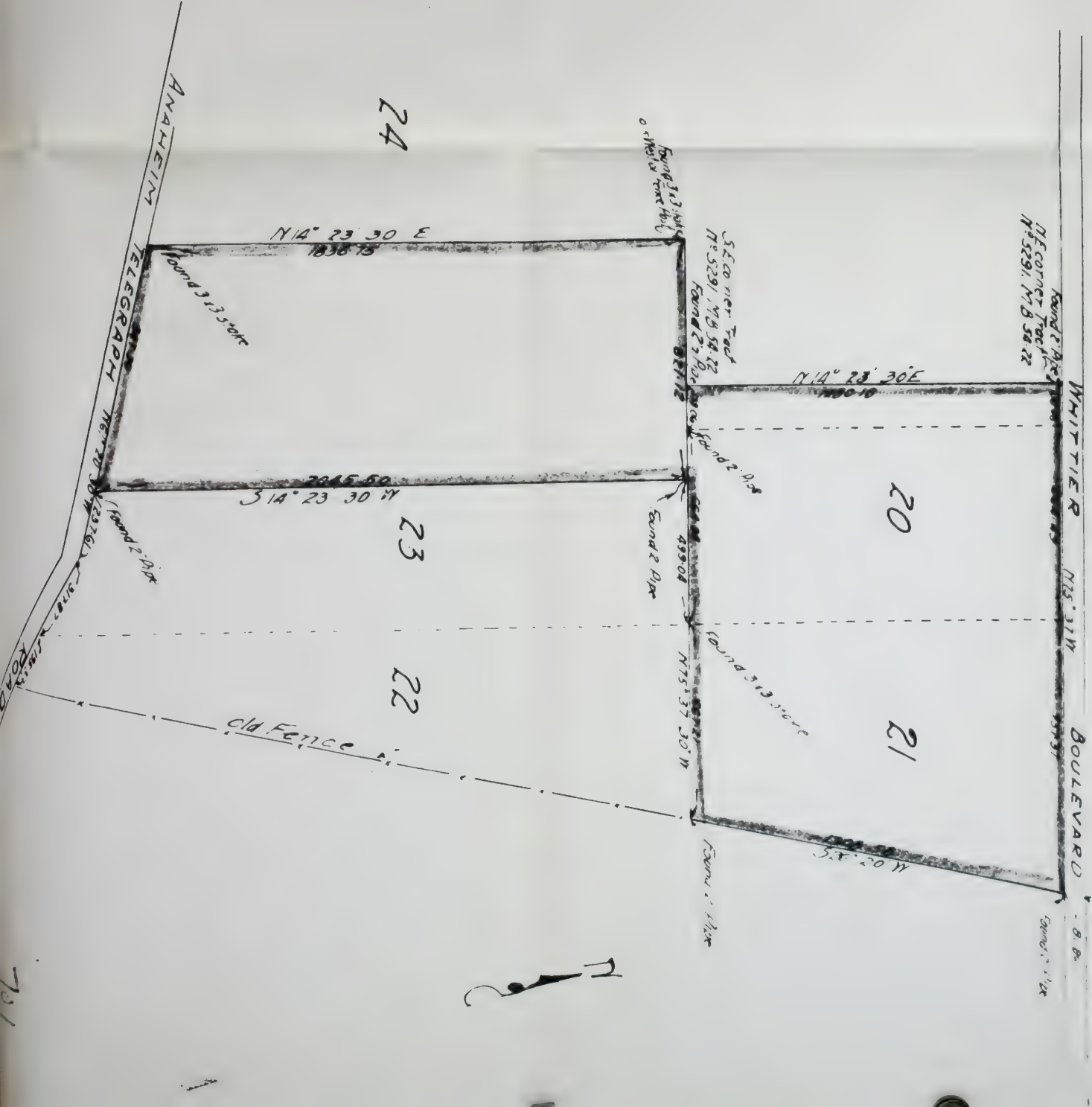
Exhibit "I"

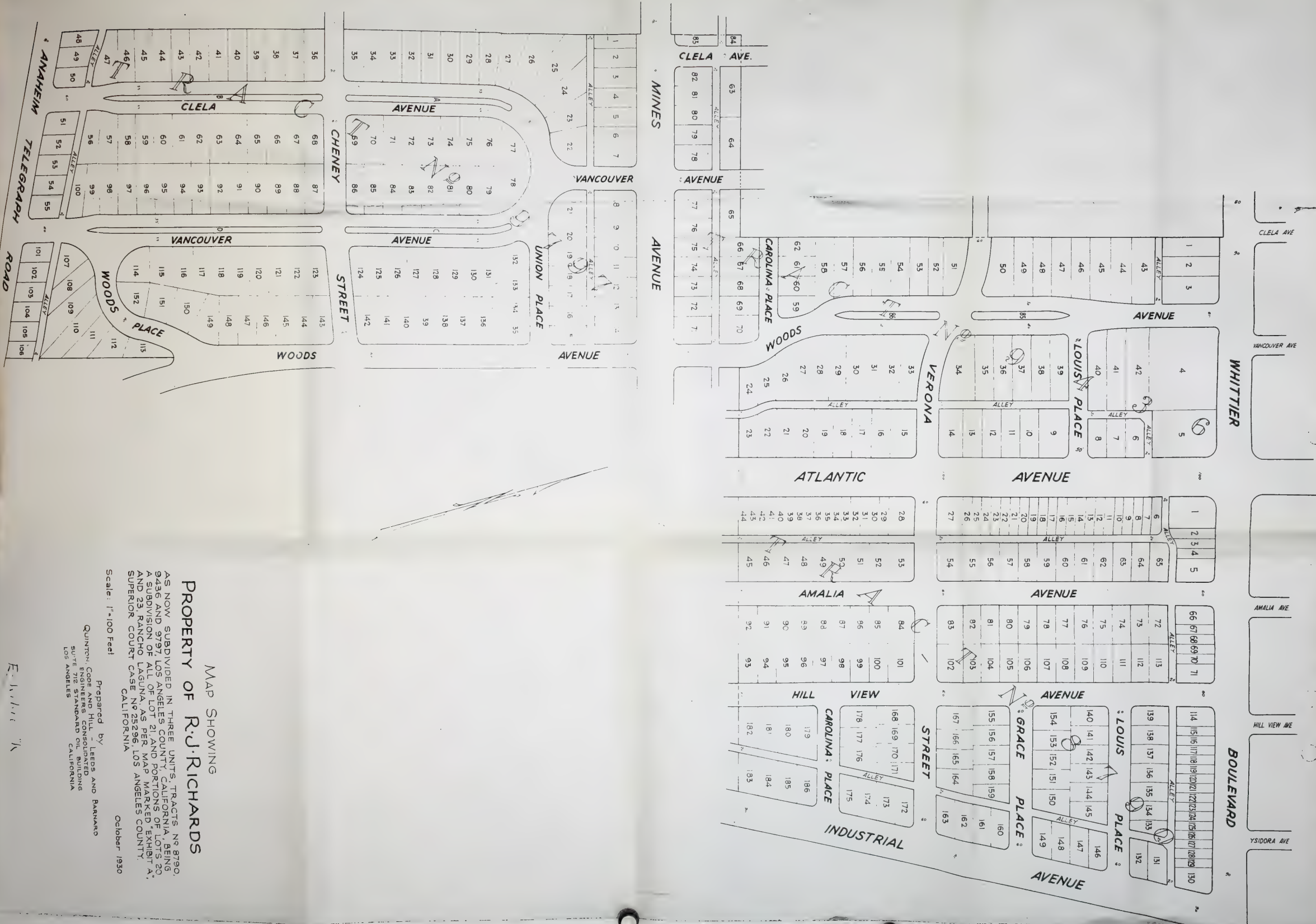
MAP SHOWING PROPERTY OF R. J. RICHARDS located between Whittier Boulevard and the Anaheim-Telegraph Road Los Angeles County, California.

LEEDS AND BARNARD
Consulting Engineers
Los Angeles, California.

Scale 400 ft. = 1 inch

April 1923





MAP SHOWING
PROPERTY OF R.J. RICHARDS

AS NOW SUBDIVIDED IN THREE UNITS, TRACTS, NO. 8790, 9436 AND 9797, LOS ANGELES COUNTY, CALIFORNIA, BEING A SUBDIVISION OF ALL OF LOT 21, AND PORTIONS OF LOTS 20 AND 23, RANCHO LAGUNA, AS PER MAP MARKED "EXHIBIT A", SUPERIOR COURT CASE NO. 25296, LOS ANGELES COUNTY, CALIFORNIA

Scale: 1"=100 Feet
October 1930

Prepared by
J. E. BARNARD
ENGINEERS AND ARCHITECTS
SUITE 702, STANDARD BUILDING
LOS ANGELES, CALIFORNIA

The affidavit of R. J. Richards dated September 15, 1933, is in the words and figures as follows:

STATE OF CALIFORNIA,
COUNTY OF LOS ANGELES.—ss.

ROBERT JAMES RICHARDS, being first duly sworn, deposes and says:

That at no time did he ever personally sell or offer for sale any real estate in Tracts No. 8790, 9436 or 9797, in the County of Los Angeles, State of California. That affiant at no time ever solicited any person to buy any lot in said tracts or advertised said property, or any portion thereof, for sale by himself or by the bank, as trustee, or any other person; and that on each and every lot sold in said tracts there was paid a commission to the real estate agent selling the same, and that any and all contacts and business with said purchasers was handled by said agent, and that affiant at no time had anything more to do with the sale of said tracts than if said tracts had not belonged to affiant, except to fix the prices at which the same would be sold. That the real estate agent selling said real estate was at all times engaged in the real estate business, and at all times maintained an office for said purpose and was at no time under the control or direction of affiant, but carried on and conducted his business in such manner as he deemed best and without any control, guidance or direction of affiant. [136]

That in addition to the reasons stated in the affidavit of affiant dated October 20, 1930, it was

desirable for affiant to dispose of said real property because of the subdivided character of the entire neighborhood which eliminated the possibility of further farming operations by other persons in the vicinity. That affiant used the real property mentioned as a base of operations in carrying on his business as a produce shipper. Because of the ownership by affiant of such property affiant was enabled to make a better approach to other persons raising lettuce in the vicinity and in the shipping of lettuce was able to use his own product as a surplus to be shipped when the crops of other produce growers in the vicinity were not immediately available for shipment or their price was in the opinion of affiant excessive at such time. When produce similar to that being raised by affiant could no longer be raised in the neighborhood, by reason of the subdivision thereof, affiant's property did not furnish a satisfactory base for his shipping operations, since there were not other similar crops in the neighborhood to be acquired and shipped by affiant, except his own crop, and affiant could not, therefore, maintain a constant car lot shipping method which was possible when other produce growers were operating in the vicinity and affiant was enabled to use his own crops to fill up short car lot loads or supply affiant's shipping requirements when the market price of other growers' produce was excessive. [137]

That in reference to the sale of lots in the tracts above mentioned and involved in this proceeding, affiant devoted no time whatever to the sale thereof

or to any other matters in connection therewith, except to have his auditor from time to time check the amounts due from the trustee by reason of the sums received by the bank, as trustee, on account of the sales made in said trusts by P. N. Snyder, who had the exclusive handling and sale of the same during all times referred to in affiant's petition and during the times referred to in affiant's affidavit dated October 20, 1930, and above referred to.

(SIGNED) ROBERT JAMES RICHARDS.

Subscribed and sworn to before me this 15th day of September, 1933.

[Seal]

(SIGNED) MURIEL P. MONTGOMERY,
Notary Public in and for the County
of Los Angeles, State of California.

It is agreed between the parties that the foregoing statement contains all the evidence introduced at the hearing of this case before the United States Board of Tax Appeals [138] material to the issues in controversy and is intended to be filed as a part of the record on appeal this the 25 day of March, 1935.

C. E. McDOWELL,
Attorney for Petitioner.

The foregoing statement of the evidence is agreed to by the respondent.

ROBERT H. JACKSON,
Attorney for Respondent.

Approved and ordered to be filed this the 25th day of March, 1934.

(Sgd) EUGENE BLACK,

Member

United States Board of Tax Appeals.

[Endorsed]: Filed Mar. 25, 1934.

Lodged Dec. 17, 1934. [139]

[Title of Court and Cause.]

**PRAECIPE FOR RECORD
TO THE CLERK OF THE UNITED STATES
BOARD OF TAX APPEALS:**

You will please transmit and deliver to the Clerk of the United States Circuit Court of Appeals for the Ninth Circuit, copies duly certified as correct of the following documents and records in the above-entitled cause, in connection with the petition for review by the said Circuit Court of Appeals for the Ninth Circuit, hereto filed by the above-named taxpayer:

1. Docket entries of proceedings before the Board of Tax Appeals.
2. Pleadings before the United States Board of Tax Appeals by the respective parties and exhibits referred to therein and made a part thereof. [140]
3. Opinion and decision of the United States Board of Tax Appeals.

4. Petition for review, together with proof of service of notice of filing petition.

5. Statement of evidence agreed to by the parties and made a part of the record by order of the Board.

6. Orders of the Board enlarging the time for settlement, preparation and transmission of the record. (Not included in record.)

7. Stipulation by the parties designating the United States Circuit Court of Appeals for the Ninth Circuit as the Circuit Court for reviewing decision of the Board.

8. This praecipe.

(SIGNED) C. E. McDOWELL,
Attorney for Petitioner.

Service of the foregoing praecipe, together with receipt of a copy thereof, is acknowledged this the 25th day of March, 1935.

(SIGNED) ROBERT H. JACKSON,
Assistant General Counsel,
Bureau of Internal Revenue,
Attorney for Respondent.

[Endorsed]: Filed Mar. 25, 1935. [141]

[Title of Court and Cause.]

CERTIFICATE

I, B. D. Gamble, clerk of the U. S. Board of Tax Appeals, do hereby certify that the foregoing pages,

1 to 141, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of the United States Board of Tax Appeals, at Washington, in the District of Columbia, this 8th day of April, 1935.

[Seal]

B. D. GAMBLE,

Clerk,

United States Board of Tax Appeals.

[Endorsed]: No. 7835. United States Circuit Court of Appeals for the Ninth Circuit. R. J. Richards, Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Upon Petition to Review an Order of the United States Board of Tax Appeals.

Filed April 13, 1935.

PAUL P. O'BRIEN,

Clerk of the United States Circuit Court of Appeals
for the Ninth Circuit.

In the United States
Circuit Court of Appeals
For the Ninth Circuit.

R. J. Richards,

Petitioner,

vs.

Commissioner of Internal Revenue,

Respondent.

PETITIONER'S OPENING BRIEF.

C. E. McDOWELL,

Title Guarantee Bldg., 411 W. Fifth St., L. A.,

Solicitor for Petitioner.

FILED

NOV - 4 1935



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No. 7835

In the United States
Circuit Court of Appeals
For the Ninth Circuit.

R. J. Richards,

Petitioner,

vs.

Commissioner of Internal Revenue,

Respondent.

PETITIONER'S OPENING BRIEF.

STATEMENT OF THE CASE.

QUESTIONS INVOLVED AND HOW RAISED.

This case comes before this Court upon a Petition to Review a decision of the United States Board of Tax Appeals (hereinafter referred to for convenience as "Board") sustaining the Commissioner of Internal Revenue in the determination of Income Tax deficiencies against the petitioner as follows:

Years	Deficiency
1927	\$ 486.69
1928	12,552.81

The proceedings before the Board arose under a petition filed by your petitioner on February 14, 1931, for re-determination of the Commissioner's proposed deficiencies of the years given. The opinion of the Board, which is set out in full in the transcript [page 32 *et seq.*], is reported at 30 B. T. A. 1131.

The matter was submitted to the Board for determination on two affidavits of the petitioner [Tr. 51 *et seq.* and Tr. 175 *et seq.*] under a stipulation that the petitioner if called as a witness would testify as set forth in the affidavits. No other evidence was introduced and the matter was considered by the Board upon petitioner's uncontradicted affidavits.

The only issue to be determined is whether or not certain real estate acquired by the petitioner in the vicinity of Los Angeles for use in petitioner's business of producing, packing and selling lettuce and other vegetables and subdivided and sold, more than two years after acquired, and during the taxable years 1927 and 1928, constituted "Capital Assets" within the meaning of sections 208 (a) (8) of the Revenue Act of 1926, and sections 101 (c) (8) of the Revenue Act of 1928.

These sections are substantially similar and section 208 (a) (8) reads as follows, in so far as is applicable to this controversy:

(8) "The term 'capital assets' means property held by the taxpayer for more than two years (whether or not connected with his trade or business) but does not include stock in trade of the taxpayer or other property of a kind which would properly be included in the inventory of the taxpayer if

on hand at the close of the taxable year, *or property held by the taxpayer primarily for sale in the course of his trade or business.*" (The italics are counsel's.)

The real property involved was acquired by petition as acreage, but was subsequently subdivided and sold by petitioner in a manner more particularly hereinafter set forth, when it became impractical for petitioner to continue to use such acreage in the carrying on of his business. The Commissioner argued and the Board determined in effect that although the petitioner was at all time continuing to operate his business of producing, packing and selling such lettuce and other vegetables, nevertheless by selling as subdivided lots his farm acreage then no longer useful in his business petitioner became engaged in a new business, to-wit, the "real estate business", and the real property was held by him "primarily for sale" in the course of this "real estate business".

Petitioner contended that the sale of such real estate was purely an incident of petitioner's real business of producing, packing and selling lettuce and other vegetables to which petitioner was devoting substantially all of his time, and that the financial success of such business required the liquidation of the particular real property involved, and that by so doing petitioner did not engage in the "real estate business" or any other new business. The respondent further contended that all gains derived by petitioner from the sale of such real estate should be treated as "capital net gain" and taxed at the 12½% rate rather than under the ordinary normal and surtax rate applied to the remainder of petitioner's income. The petition of your petitioner was contested by the Commissioner and

the Board, in an opinion written by Judge Marquette, sustained the Commissioner's objections on the basis of *Willard Pope*, 28 B. T. A. 1255, which is another opinion written by Judge Marquette. This decision was recently reversed by the United States Circuit Court of Appeals for the Sixth Circuit in *Pope v. Commissioner*, 77 Fed. (2d) 599, and is no longer an authority.

STATEMENT OF FACTS.

In the following statement of facts petitioner is including *verbatim* portions of the Board's findings of fact in *italics*, the additions thereto in ordinary type are from the uncontradicted affidavits of your petitioner:

"The petitioner and his wife made joint income tax returns for the years before us, and that the real property involved was acquired by them as joint tenants with the right of survivorship. Since prior to 1920 the petitioner, for himself or as a member of a partnership, has been engaged in the business of raising, packing, buying and marketing farm products, particularly lettuce. About September 15, 1920, petitioner and his wife acquired title to approximately 47 acres of land in Los Angeles County, California. About April 30, 1921, they acquired another tract adjoining the above tract, containing about 4 acres. About March 11, 1922, they acquired title to a third piece of land adjacent to the foregoing tracts. These tracts of land at the time of acquisition lay in a very productive farming area and were used by the petitioner in the raising of lettuce and sometimes chicory and endive. They were surrounded by farm lands producing these same vegetables and because of the ownership by petitioner of

such property petitioner was enabled to make a better approach to other persons raising lettuce in the vicinity and in the shipping of lettuce was able to use his own product as a surplus to be shipped when the crops of other growers in the vicinity were not immediately available for shipment or their price was, in the opinion of petitioner, excessive at such time. [Tr. 176.]

“In 1921 the petitioner erected buildings and other structures on not over three and one-half acres of these lands, which were thereafter used by him as a combined office and residence.

“After the petitioner acquired these properties there was a great deal of real estate activity in the lands between his property and the boundary of the city of Los Angeles. The intervening property began to be subdivided and sold, with the result that the petitioner’s property rapidly increased in value until it arrived at a value in excess of \$4,000.00 an acre without improvements. Taxes and assessments for local improvements also increased. The taxes on this property in 1920 were \$657.84 and for 1924 were \$5,903.22 in addition to which the petitioner was required to pay \$4,479.95 in 1924 on account of special assessments. This rise in prices” and the upkeep by way of taxes, assessments for local improvements and similar charges made the holding of said lots [Tr. 55] “and the adjacent lands for gardening purposes unprofitable” and when produce similar to that being raised by petitioner could no longer be raised in the neighborhood by reason of the subdivision thereof petitioner’s property did not furnish a satisfactory base for his shipping operations since there were no other similar crops in the neighborhood to be ac-

quired and shipped by petitioner except his own crop and petitioner could not therefore maintain a constant car lot shipping method which was possible when other produce growers were operating in the vicinity and petitioner was enabled to use his own crops to fill up short car lot loads or supply petitioner's shipping requirements when the market price of other grower's produce was excessive. [Tr. 176.]

In 1925 petitioner determined to subdivide a part of the first parcel of land which he had purchased. In pursuance of this plan on July 15, 1925, he conveyed a portion of the property to the Security Trust & Savings Bank of Los Angeles (now Security First National Bank of Los Angeles) hereinafter referred to as the bank, which accepted it in trust to secure a note of \$28,500 which petitioner and his wife owed the bank, and upon further trust to subdivide and sell the property conveyed. Under the deed of trust petitioner and his wife agreed to pay all taxes and assessments levied on the property, to pay principal and interest on all indebtedness secured by the trust, to pay all claims, liens and encumbrances and defend all suits affecting the property, to pay for all improvements ordered by him or his agent, and to file with the trustee a copy of each contract for improvements to be placed on the property. The property was to be subdivided and improved by the petitioner and his wife.

The deed of trust contained provisions which permitted the trustee, upon default of petitioner and his wife in paying the above amounts, to pay them itself, and gave it recourse against the property. The trustee was authorized to rent, sell and convey the property or any part

thereof to such persons and at such times as it deemed best, provided the sale prices of the land should not be less than those indicated in the schedule to be filed with the deed of trust. The proceeds received from the sales were to be used to pay commissions and to release liens, the balance to go in what was termed a general fund, out of which the cost and expense of the trust and certain other expenses were to be paid, and what remained over was to be paid to the petitioner and his wife. The deed of trust recites that at the request of the petitioner and his wife it appointed P. N. Snyder "as their exclusive agent to subdivide and improve, and to solicit and obtain purchasers for such part of said property" as was subdivided. He was paid a commission, out of which he was to pay for advertising and other selling expenses of himself and his subagents. Among the duties assumed by the agent was the general care and custody of the subdivided property, and of all improvements placed upon the property, which included the installation of gas, water and electricity. The trustee was not required to procure any insurance on any building upon the property, or to collect or disburse any rentals therefrom. These duties were to be performed by the petitioner and his wife.

Upon payment in full of the indebtedness secured by the deed of trust and at the request in writing of petitioner and his wife, the trustee was given authority to close and terminate the trust, but was not required to do so as long as any of the covenants contained in any deed remained unperformed. The petitioner and his wife furnished the trustee a list of the minimum prices at which the lots were to be sold. The number of lots was 186.

The minimum price was \$1,250 and the maximum price was \$40,000 per lot.

The sales of lots in the first subdivision having proved satisfactory, petitioner determined to subdivide other portions of the property above described. By deed of August 6, 1926, the bank accepted the trust property previously conveyed. The provisions of this trust deed resembled the one of July 15, 1925. Afterward, the petitioner and his wife determined to subdivide and sell the remaining portion of the property purchased as hereinabove set forth, and by deed of trust dated January 12, 1927, the bank accepted such property on practically the same trusts as those provided in the deed of trust of July 15, 1925.

The principal reason for the above conveyances was to have all deeds on lots promptly executed, especially in the absence of the petitioner from Los Angeles. The number of lots in the second subdivision above set forth was 82. The number of lots in the third subdivision was 152. In the third subdivision the minimum price for the lots was \$1, 200 and the maximum was \$15,000. Under each of the deeds, Snyder was appointed by the bank as petitioner's exclusive agent, at their request, for a term of eight months, with the right to serve eight months more upon achieving certain results, and upon the termination of his employment the trustee was to appoint as agent for the petitioner and his wife such person as they directed, all sales, however, to be subject to the approval of the trustee of the bank. That in the sale of lots in the three tracts petitioner took no active part but the promotion, advertising and sale of said lots was handled by the said P. N. Snyder who conducted his advertising campaign in such

a manner as to create the impression he was a subdividor and developer of the property above described to such an extent that the general public believed the said P. N. Snyder was the owner thereof and did not know that your petitioner had any interest in and to the same. [Tr. 63.]

The petitioner's business of producing, packing and selling lettuce and other vegetables increased from year to year, and he substituted, either by lease or purchase, farming properties for the properties which he subdivided.

Petitioner at no time ever solicited any person to buy any lots in said tracts or advertised any portion thereof for sale by himself or by the bank as trustee or any other person and that on each and every lot sold in said tracts there was paid a commission to the real estate agent selling the same and that any and all contacts and business with said purchasers were handled by said agent and that petitioner at no time had anything more to do with the sale of said tracts, that if said tracts had not belonged to petitioner, except to fix the price at which the same could be sold. The real estate agent selling said lots was at all times engaged in the real estate business and at all times maintained an office for said purpose and was at no time under the control or direction of petitioner but carried on and conducted his business in such manner as he deemed best and without any control, guidance or direction of petitioner. [Tr. 175.]

That at no time has petitioner purchased any real estate for subdivision and sale. That at the time petitioner determined upon the subdividing and sale of said three tracts petitioner did not intent to go into the real estate business or to purchase any additional property for subdivision or sale. [Tr. 62.]

That petitioner has never engaged in the real estate business or in the business of buying and selling real estate, nor has petitioner ever been a dealer in real estate, nor licensed as a broker or salesman under the laws of the state of California, or elsewhere to buy and/or sell real estate, nor is petitioner a member of any real estate board or other organization of persons engaged in the sale of real estate, nor has petitioner any place of business from which he carries on or conducts a real estate business, or the buying and selling of real estate, nor has petitioner ever made purchases or sales or dealt in any way with real estate for third persons. [Tr. 52.]

Board's Conclusions and the Assignments of Error.

The ultimate question of law to be determined upon this appeal is whether the liquidation of real property through sales by your petitioner in the manner set forth in the statement of facts places your petitioner in the "real estate business" although such real property was no longer desirable for use in connection with your petitioner's business of producing, packing and selling vegetables and the liquidation by sale was indirectly occasioned by conditions and circumstances over which your petitioner had not the slightest control. If this court believes under the admitted facts in the case at bar, your petitioner was engaged in the real estate business, then the position of respondent should be sustained. If your Honorable Court, however, believes that the sale of the real property involved was only an incident to the successful management

of petitioner's admitted business of producing, packing and selling vegetables, then the decision of the Board should be reversed.

The assignments of error appear in the transcript of record [Tr. 47 *et seq.*] As they are not extensive they are, for the convenience of the court, here stated as follows:

1. The Board erred in its conclusion that your petitioner was engaged, during the years involved, in any other business than the business of producing and marketing vegetables and other farm products.

2. The Board erred in its conclusion that the real property constituting the tracts above mentioned, required by the petitioner and his wife, in such business of producing and marketing farm products was ever devoted to a purpose not connected with such business.

3. The Board erred in its conclusion that the sale, through said trusts, by your petitioner of said real property was not a partial liquidation of petitioner's said business in so far as said business required the use or ownership of said lots.

4. The Board erred in its conclusion that the issue raised by petitioner was whether petitioner in selling lots in said tracts, during the years 1927 and 1928, through said trusts, was engaged in a business.

5. The Board erred in its conclusion that the lots in said tracts, sold through said trusts, were held by the petitioner primarily for sale in the course of his business.

6. That the Board erred in its conclusion that petitioner is not entitled to the benefits of section 208 of the Revenue Act of 1926, and section 101 of the Revenue Act of 1928, in computing and determining the income taxes of your petitioner during the years 1927 and 1928, with reference to the profits made by your petitioner from the sale of lots in the tracts above mentioned, through such trusts.

7. That the Board erred in redetermining a deficiency in income taxes against your petitioner in the sum of \$486.69 for the year 1927, and in the sum of \$12,552.81 for the year 1928.

BRIEF OF ARGUMENT.

The rules of law to be discussed herein may be summarized as follows:

1. The sections of the Revenue Act of 1926 and the Revenue Act of 1928, whose interpretation is involved in this decision, are remedial in character.

2. That within the clear intention of these sections your petitioner did not engage in a new business by selling assets of his admitted business when the proper management of such latter business required such sale.

3. That the decision of the Board in *Willard Pope*, 28 B. T. A. 1255, which the Board considers controlling in the case at bar has been overruled in *Pope v. Commissioner*, 77 Fed. (2d) 599.

4. That petitioner's sale of assets was in the nature of a liquidation and not in a sale in the course of business.

I.

The Sections of the Revenue Act of 1926, and the Revenue Act of 1928 Whose Interpretation Is Involved in This Decision Are Remedial in Character.

Prior to the Revenue Act of 1921 there was no provision in the various Acts similar to section 208 (a) (8). Then the net profit made by a taxpayer as the result of a sale of an asset held by the taxpayer for a number of years was considered income for the year in which the sale or other disposal was made. In many instances this prevented the sale by owners of greatly appreciated property and prevented this property from passing into productive hands, and apparently in considering the relief of this situation Congress felt that it would be better to tax such profits at a flat rate of $12\frac{1}{2}\%$ rather than to receive no taxes at all. The printed report of the Congressional Joint Committee on Internal Revenue taxation then considering this matter states (p. 42) in part, as follows:

“Taxpayers who realize capital gains fall into two classes—(1) those who *sell property not primarily purchased for purpose of resale*, and (2) those who *sell property purchased for the purpose of resale*. In the former group fall a large number of persons who sell residences, factories, land, and investments often held for a period of many years. In the latter group fall those who *buy* stocks, bonds, and other

property *in the expectation of selling on a rising market.* (Italics are counsel's.)

“From the viewpoint of the first group the capital-gains tax must be regarded as a very needful remedial provision. Their sales are often made under some degree of compulsion, such as the necessity of moving to a new neighborhood, retirement from business, settlement of interests of cotenants, etc. Where property has been held for 10 or 15 years and is then sold, the result may be the immediate conversion into cash of a relatively large profit accumulated over a long period of time. To tax that profit at graduated surtax rates, designed primarily to measure the tax on a single year's profit, is obviously unduly burdensome. If it were practicable to segregate such transactions, consideration might properly be given to their special treatment.”

That taxpayer falls in the first class above mentioned is apparent. That he is one of those who should be benefited by such remedial legislation seems clear. The real property involved in this controversy was not purchased for “re-sale,” and the disposal of the same was under a “degree of compulsion,” *i. e.*, the necessity of removing to other locations for the purposes of conducting petitioner's admitted business in a profitable manner. The tax levied is “unduly burdensome.”

II.

**That Within the Clear Intention of These Sections
Your Petitioner Did Not Engage in a New Business
by Selling Assets Under His Admitted Business
When the Proper Management of Such
Latter Business Required Such Sale.**

It is conceded by respondent that petitioner was in the business of producing, packing and selling vegetables, which business for convenience we will hereafter refer to as the "produce business." It is not denied by respondent that a reasonable and proper management of such business required the sale by your petitioner of the real estate involved. Nor is it denied by petitioner that the real property involved was subdivided by your petitioner and held thereafter primarily for sale since it could not be practically used in the conduct of petitioner's produce business. This leaves the question open as to whether or not the real property was for sale "in the course of his trade or business." *It is on this last phrase only* that petitioner and respondent differ. Any asset in any business which is no longer of any use in the business and which the operator of the business desires to dispose of, is of course held "primarily" for sale thereafter. A sale always consists of an offer and an acceptance, the offer may be made by the buyer or by the seller and the acceptance given by the other party. If property is held "primarily for sale" it is held subject to an open offer of the owner to dispose of the same. If the owner is willing to sell but making no special effort to sell his property, possibly the property might not be held "primarily for sale." So far as the income or profits is concerned, it should make no difference whether the owner was openly

offering his property for sale or secretly awaiting an offer from some buyer. The manner of the sale, or the efforts of the owner to dispose of the property would therefore not seem to be the standard for determination in this matter.

Nor does it appear that the term "in the course of his trade or business" would apply to sales of assets by a taxpayer when such sales are not essential to the conduct of the business itself. For example in a produce business it would be necessary in the "course" of such business to buy and sell vegetables; in the "course" of a dry goods business it would be necessary to buy and sell dry goods; in the course of a real estate business it would be necessary to buy and sell real estate. The term "course" means a method of procedure. The method of procedure by which petitioner conducted his "produce business" might require the buying or selling of real estate, but such transactions would not be essential to the produce business or make petitioner in the real estate business. It would be equally absurd to say that a third person was engaged in the "produce business," if his method of conducting a "real estate" business involved the buying and selling of real estate, which had vegetables growing on it.

The Board in its decision points out that a taxpayer may be engaged in more than one business. This, of course, is true, but your petitioner respectfully contends that he does not engage in a second business, to-wit, the "real estate business" when as a proper incident to the produce business he sells an asset no longer useful or desirable in such latter business. That he sells it in a manner which he believes most profitable to him does not

change the situation nor is the situation changed by the magnitude of the operations.

As is stated by the Circuit Court of Appeals in the Second Circuit in *Commissioner v. Morriss Realty Co. Trust No. 2*, 68 Fed. (2d) 648, at 650:

“Trust No. 2, for the *purpose of liquidation*, owned certain tracts of land which the settlers designed to be sold so as to net the most money for distribution among the beneficiaries according to the respective interests. They were located in the environs of Granite City; their sale for purely agricultural purposes would not have brought a very large return, being located as they were adjacent to an industrial center; it was clear that their greatest value lay in subdividing and selling them as city or town lots. To do so would necessarily take a considerable period of time, and the settlers and trustees had a perfect right to sell the assets of the trust estate, the lands in question, in the most satisfactory way in order to turn the property into cash for the use of the beneficiaries and give them the benefit of the largest measure of distribution.”

The court then held that such activities did not show such trust to be carrying “on some business enterprise.”

If your petitioner was engaged in more than one business it would seem that there should be a clear delineation between the two and that one should not be a mere incident to the other. In any business there invariably comes a time when capital assets of the business must be replaced or renewed. A factory becomes antiquated and must be sold or rebuilt; machinery becomes obsolescent and must be disposed of as junk or remodeled to bring it up to date. The

disposal of any such an asset is always a problem, and the taxpayer should have the right to dispose of the same in the manner most profitable to himself. It is true that the manufacturer selling obsolescent machinery is selling junk, but he is not engaged in the junk business unless he maintains a stock of trade from which his sales are being replenished.

III.

That the Decision of the Board in Willard Pope, 28 B. T. A. 1255, Which the Board Considers a Controlling Decision in the Case at Bar Has Been Overruled in Pope v. Commisisoner, 77 Fed. (2d) 599.

The opinion of the Board in this matter was written by Judge Marquette, who also wrote the opinion in *Willard Pope, supra*. In writing this opinion Judge Marquette apparently felt bound by his former opinion in *Willard Pope, supra*. He quotes extensively from it and arrives at the same conclusions that he had in the former opinion. Apparently Judge Marquette thought the fact that the transactions involved were not isolated transactions, that money was expended in improvements and that there was "continuity of effort. All done for gain." brought the transactions of your petitioner in subdividing and selling the real estate involved "within the concept of the term 'business.'" That the transactions of your petitioner in subdividing and selling these lots were "business" transactions of course permits of no argument. That they were conducted for a gain is admitted, but all these facts do not show that such sales were *in the course of petitioner's produce business*. The Board erred in hold-

ing that the real estate transactions of your petitioner constituted a new business, to-wit, the “real estate business,” and, therefore, the “capital assets provisions” of the Revenue Acts did not apply. A petition to review the decision of the Board in *Willard Pope, supra*, was taken to the Circuit Court of Appeals for the Sixth Circuit, and the order of the Board of Tax Appeals was unanimously reversed by that court in its decision in *Pope v. Commissioner*, 77 Fed. (2d) 599.

In this last decision it is stated:

“The sole question presented on this question is whether the evidence is legally sufficient to sustain the Board’s findings that the lands were held by petitioner primarily for sale in the course of his trade or business.”

It appears, therefore, that the questions in that decision and the instant case were identical. The court in rendering its decision disregarded all of the bases on which the Board had placed its opinion, that is, the fact that the transactions were not isolated, the expenditure of money, the continuity of effort, that the transactions were for gain, and considered only the business activities of the taxpayers, stating:

“The respondent introduced no testimony before the Board of Tax Appeals. Both of the petitioners testified that they joined other members of the syndicate in putting up the money to buy the land because they thought it was a good investment, and not for the purpose of engaging in the business of buying and selling lands. Neither of them has ever been licensed as a real estate dealer. While both held stock in the Essex Company, neither was ever active

in the company, and after they purchased the tract for the syndicate in 1920, neither ever bought or sold any real estate * * * By reason of their stock ownership in and official relation to the Essex Company the petitioners could, of course, have engaged in the real estate business, but in our opinion their activities in the company were not such as to justify an inference that they were so engaged. We think the purchase of the land is to be treated as an investment, and the investment having been made, the sale through real estate brokers is to be regarded as a conversion of the capital assets and not a sale by the petitioners in the course of a trade or business.

The order of the Board of Tax Appeals is reversed, and the cause remanded for further proceedings.”

In the case at bar the petitioner respectfully submits that the decision of the Circuit Court of Appeals for the Sixth Circuit should be followed to create a uniformity of opinion. Your petitioner certainly did not buy the land involved for re-sale or for the purpose of engaging in the business of buying and selling lands. [Tr. 54.] Petitioner never did engage in the real estate business. [Tr. 176.] All sales were likewise handled through a real estate broker [Tr. 63] and the same conclusion should be arrived at by this court, to wit: That the sales made by your petitioner are “to be regarded as a conversion of capital assets and not a sale by your petitioner in the course of a trade or business.”

IV.

That Petitioner's Sale of Assets Was in the Nature of a Liquidation and Not in a Sale in the Course of Business.

It has been unanimously held by the decisions of the various Circuit Courts of Appeals that a liquidation of assets does not constitute doing business. Your petitioner feels that the sale of the real property in question constituted a liquidation of those particular assets. The Board in its opinion disposes of that contention of your petitioner as follows:

“We may here dispose of the issue raised by the petitioner that in disposing of the lots by sale he was liquidating his business of farming, or at least a part of it. He relies on *Trustees for the Creditors and Stockholders of Gonzolus Creek Oil Co.* (dissolved), 12 B. T. A. 310; *Wilson Syndicate Trust*, 14 B. T. A. 508; *Dauphin Deposit Trust Co., Trustee*, 21 B. T. A. 1214; *G. F. Sloan*, 24 B. T. A. 61; *Blair v. Wilson Syndicate Trust*, 39 Fed. (2d) 43; *White v. Hornblower*, 27 Fed. (2d) 277. We do not perceive the relevancy of these cases. Not only has the petitioner not liquidated his business of farming, but, as we read the record, he has enlarged it. What he has done is to take certain assets individually owned and devoted them to a new purpose.”

It is to be noted that in the Board's comments on your petitioner's contention the Board has unanimously accepted the point of your petitioner that he is engaged in the business of “farming” or the produce business, as we have referred to it, but the Board refuses to follow petitioner in the contention that the sale of the real property involved

was an incident of the produce business. Petitioner does not contend that he was liquidating his produce business. That is a going business and requires the use of land for its successful operation. This land your petitioner has on some occasions leased and on others bought, but the land itself when no longer valuable in petitioner's business has been liquidated by petitioner and such liquidation does not create a new "business" and is actually not "doing business" at all. See:

Blair v. Wilson Syndicate Trust (Fifth Circuit),
supra;

White v. Hornblower (First Circuit), *supra*;

Commissioner v. Atherton, 50 Fed. (2d) 740
(Ninth Circuit);

Commissioner v. Morris Realty Co. Trust No. 2
(Seventh Circuit), *supra*.

Conclusion.

The questions involved in this appeal are solely questions of law; there is no conflict in the evidence and the findings of the Board in the decision from which this petition and review is taken are favorable to the petitioner. It is clear that petitioner was never engaged in the "real estate business" or any other business but the "produce business." It is equally certain that the sale of real estate made by him hereunder was purely incidental to the proper conduct of such "produce business." That such sales also proved profitable to petitioner does not change the situ-

ation, but only speaks favorably for petitioner's general business astuteness. That there were many sales is not important. In order, therefore, that the remedial character of the statute involved may be carried out and that there may be uniformity in the decisions of our Circuit Courts your petitioner requests that your Honorable Court follow the Circuit Court of Appeals for the Sixth Circuit in *Pope v. Commissioner, supra*, and reverse the judgment of the Board of Tax Appeals herein complained of.

C. E. McDOWELL,

Solicitor for Petitioner.

No. 7835

**In the United States Circuit Court of
Appeals for the Ninth Circuit**

R. J. RICHARDS, PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

**ON PETITION FOR REVIEW OF DECISION OF THE UNITED
STATES BOARD OF TAX APPEALS**

BRIEF FOR THE RESPONDENT

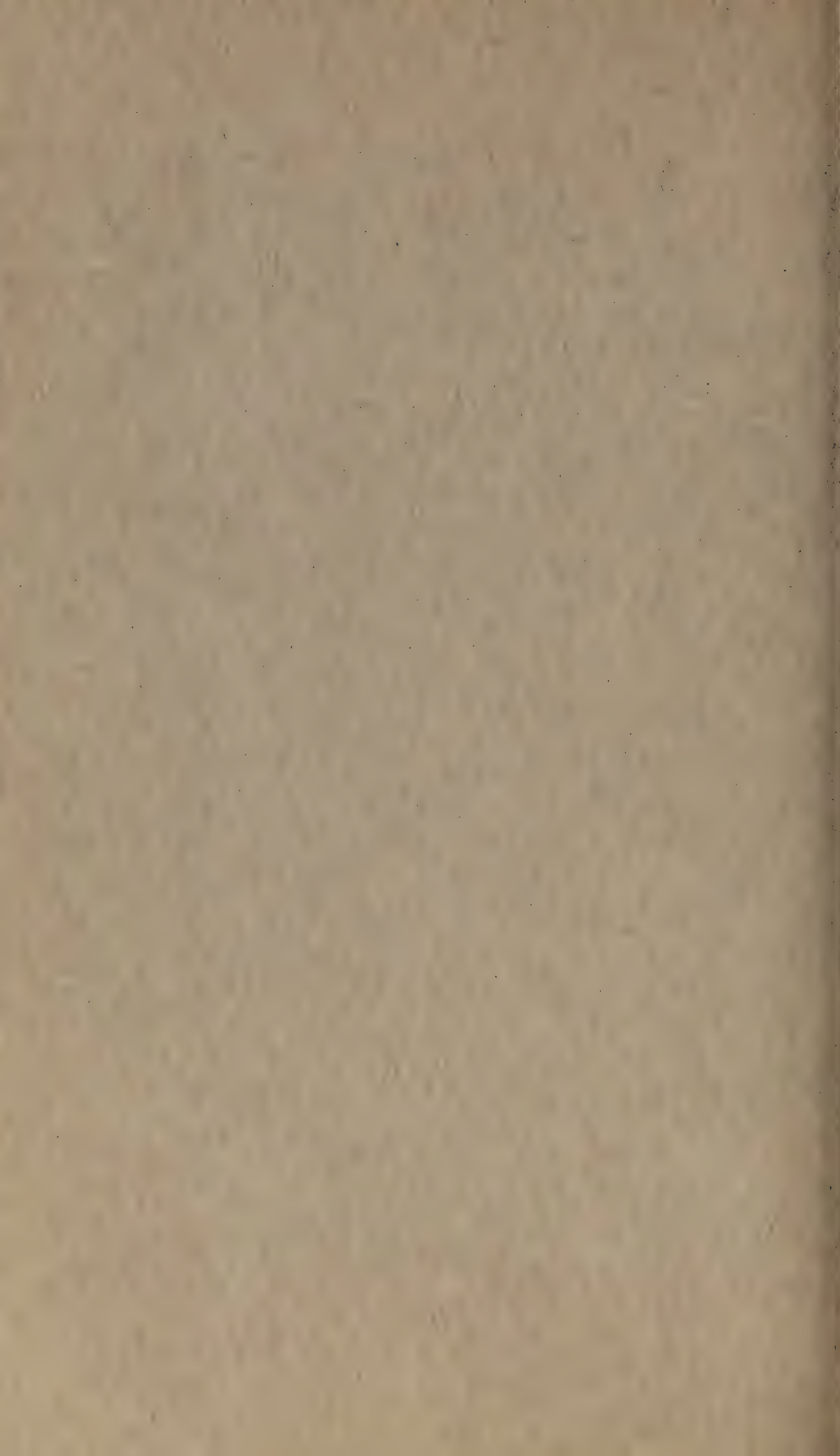
FRANK J. WIDEMAN,
Assistant Attorney General.

SEWALL KEY,
JOSEPH M. JONES,
Special Assistants to the Attorney General.

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PAUL R. CORRIE



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(I)

In the United States Circuit Court of Appeals for the Ninth Circuit

No. 7835

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v.

COMMISSIONER OF INTERNAL REVENUE, RESPONDENT

*ON PETITION FOR REVIEW OF DECISION OF THE UNITED
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OPINION BELOW

The only previous opinion in the present case is that of the United States Board of Tax Appeals (R. 32-43), which is reported in 30 B. T. A. 1131.

JURISDICTION

This petition for review involves income taxes for the years 1927 and 1928 in the respective sums of \$486.69 and \$12,552.81, and was taken from a decision of the Board of Tax Appeals entered July 12, 1934 (R. 43). The case is brought to this Court by petition for review filed September 28, 1934 (R. 45-48), pursuant to the provisions of Sections 1001-1003 of the Revenue Act of 1926, c. 27, 44 Stat. 9, as amended by Section 1101 of the Revenue Act of 1932, c. 209, 47 Stat. 169.

QUESTION PRESENTED

Where the taxpayer subdivided and improved three successive tracts of land, which operations continued over a period of at least three years, were the lots held by the taxpayer primarily for sale in the course of business, or were they capital assets within the meaning of the capital gain provisions?

STATUTE INVOLVED

Revenue Act of 1928, c. 852, 45 Stat. 791:

SEC. 101. CAPITAL NET GAINS AND LOSSES.

(a) *Tax in case of capital net gain.*—In the case of any taxpayer, other than a corporation, who for any taxable year derives a capital net gain (as hereinafter defined in this section), there shall, at the election of the taxpayer, be levied, collected, and paid, in lieu of all other taxes imposed by this title, a tax determined as follows: a partial tax shall first be computed upon the basis of the ordinary net income at the rates and in the manner as if this section had not been enacted and the total tax shall be this amount plus 12½ per centum of the capital net gain.

* * * * *

(c) *Definitions.*—For the purposes of this title—

* * * * *

(8) “Capital assets” means property held by the taxpayer for more than two years (whether or not connected with his trade or business), but does not include stock in trade of the taxpayer or other property of a kind

which would properly be included in the inventory of the taxpayer if on hand at the close of the taxable year, or property held by the taxpayer primarily for sale in the course of his trade or business. * * *

(Section 208 (a) (8) of the Revenue Act of 1926 is substantially the same as the section quoted above.)

STATEMENT

The material facts as found by the Board (R. 33-38) are as follows:

The petitioner and his wife made joint income-tax returns for the years 1927 and 1928. The real property involved was acquired by them as joint tenants with the right of survivorship.

Since prior to 1920 the petitioner, for himself or as a member of a partnership, has been engaged in the business of raising, packing, buying, and marketing farm products, particularly lettuce. About September 15, 1920, petitioner and his wife acquired title to approximately forty-seven acres of land in Los Angeles County, California. About April 30, 1921, they acquired another tract adjoining the above trust, containing about four acres. About March 11, 1922, they acquired title to a third piece of land adjacent to the foregoing tracts. These tracts of land at the time of acquisition lay in a very productive farming area and were used by the petitioner in the raising of lettuce and sometimes chicory and endive.

After the petitioner acquired these properties there was a great deal of real-estate activity in the lands between his property and the boundary of the city of Los Angeles. The intervening property began to be subdivided and sold, with the result that the petitioner's property rapidly increased in value until it arrived at a value in excess of \$4,000 an acre without improvements. Taxes and assessments for local improvements also increased. This increase made the use of these lands and the adjacent lands for gardening purposes unprofitable.

In 1925 petitioner determined to subdivide a part of the first parcel of land which he had purchased. In pursuance of this plan on July 15, 1925, he conveyed a portion of the property to the Security Trust & Savings Bank of Los Angeles, hereinafter referred to as the bank, which accepted it in trust to secure a note of \$28,500 which petitioner and his wife owed the bank, and upon further trust to subdivide and sell the property conveyed. Under the deed of trust (R. 72-110) petitioner and his wife agreed to pay all taxes and assessments levied on the property, to pay principal and interest on all indebtedness secured by the trust, to pay all claims, liens, and encumbrances and defend all suits affecting the property, to pay for all improvements ordered by him or his agent, and to file with the trustee a copy of each contract for improvements to be placed on the property. The property was to

be subdivided and improved by the petitioner and his wife.

The deed contained provisions which permitted the trustee, upon default of petitioner and his wife in paying the above amounts, to pay them itself, and gave it recourse against the property. The trustee was authorized to rent, sell, and convey the property or any part thereof to such persons and at such times as it deemed best, provided the sale prices of the lands should not be less than those indicated in the schedule to be filed with the deed. The proceeds received from the sales were to be used to pay commissions and to release liens, the balance to go in what was termed a general fund, out of which the cost and expenses of the trust and certain other expenses were to be paid, and what remained over was to be paid to the petitioner and his wife.

The deed recites (R. 84) that at the request of the petitioner and his wife it appointed P. N. Snyder "as their exclusive agent to subdivide and improve, and to solicit and obtain purchasers for such part of said property" as was subdivided. He was paid a commission, out of which he was to pay for advertising and other selling expenses of himself and his subagents. Among the duties assumed by the agent was the general care and custody of the subdivided property, and of all improvements placed upon the property, which included the installation of gas, water, and electricity. The trustee was not required to procure any insurance on

any building upon the property, or to collect or disburse any rentals therefrom. These duties were to be performed by the petitioner and his wife.

Upon payment in full of the indebtedness secured by the deed and at the request in writing of petitioner and his wife, the trustee was given authority to close and terminate the trust, but was not required to do so as long as any of the covenants contained in any deed remained unperformed. The petitioner and his wife furnished the trustee a list (R. 111-114) of the minimum prices at which the lots were to be sold. The number of lots was 186. The minimum price was \$1,250 and the maximum price was \$40,000 per lot.

The sales of lots in the first subdivision having proved satisfactory, petitioner determined to subdivide other portions of the property above described. By deed of August 6, 1926, the bank accepted in trust property previously conveyed. The provisions of this trust deed (R. 114-143) resembled the one of July 15, 1925. Afterward, the petitioner and his wife determined to subdivide and sell the remaining portion of the property purchased as hereinabove set forth, and by deed of trust (R. 144-171) dated January 12, 1927, the bank accepted such property on practically the same trusts as those provided in the deed of July 15, 1925.

The principal reason for the above conveyances was to have all deeds on lots promptly executed, especially in the absence of the petitioner from Los

Angeles. The number of lots in the second subdivision above set forth was eighty-two. The number of lots in the third subdivision was one hundred fifty-two. In the third subdivision the minimum price for the lots was \$1,200 and the maximum was \$15,000. Under each of the deeds, Snyder was appointed by the bank as petitioner's exclusive agent, at their request, for a term of eight months, with the right to serve eight months more upon achieving certain results, and upon the termination of his employment the trustee was to appoint as agent for the petitioner and his wife such person as they directed, all sales, however, to be subject to the approval of the trustee of the bank.

The petitioner's business of producing, packing, and selling lettuce and other vegetables increased from year to year, and he substituted, either by lease or purchase, farming properties for the properties which he subdivided.

The petitioner, himself, has never taken part in the subdivision or the sale of the lots in the subdivisions, all of which was done by Snyder. Except as herein set forth, the petitioner has never engaged in the business of buying and selling real estate or dealt therein. He has not been licensed as a broker to buy or sell real estate.

The Board found that the lots were held by the taxpayer primarily for sale in the course of his business, and concluded that he was not entitled to the benefits of Sections 208 of the Revenue Act of 1926, and 101 of the Revenue Act of 1928.

ARGUMENT

The pertinent portion of the statute quoted above defines capital assets as property “held by the taxpayer for more than two years * * * but does not include * * * property held by the taxpayer primarily for sale in the course of his trade or business * * *.” The taxpayer seeks to come within the capital gain provisions so as to pay income tax on the profits in question on the level rate of 12½ percent rather than on the normal sliding scale of tax and surtax on individual incomes. The statutory definition excludes from capital assets property held primarily for sale in the course of a trade or business. The lots of the subdivision here involved were admittedly held by the taxpayer primarily for sale, so the only question before the court is whether or not the taxpayer was engaged in a business.

When the operation of the properties for farming purposes became unprofitable, the taxpayer decided to subdivide and sell them (R. 56). In doing this he engaged in three separate and distinct subdivision projects, all of which extended over the period of time involved in the present proceedings. The subdivision of the property, which was then adapted only to farming, was not a simple business operation. (See charts, R. 114, 144, 174.) Many things were involved, such as engineering features, drainage, sewers, grading and paving of streets, sidewalks, curbs, the subdivision of the property into lots so as to afford access to the vari-

ous conveniences; and there were involved matters of organization, sales, advertising, the furnishing of certificates of title, financial arrangements, and numerous other details that called for judgment and management (R. 78).

When the taxpayer saw that the first project was going over successfully, he entered upon the second project, and then later upon the third. These were operations of considerable magnitude. The total number of lots in the three subdivisions was four hundred and twenty, and the prices ranged from \$1,200 to \$40,000 per lot (R. 37). The operations were spread over a period of four or five years. The Government submits that they constitute business operations on the part of the taxpayer within the meaning of the pertinent revenue statute.

The fact that the taxpayer engaged a selling agent is immaterial. The selling was a relatively simple feature of the business operation. The burden was upon the taxpayer to formulate and execute the plans for subdividing and improving the property preparatory to the sales. In any event the acts of the agent in such a case are the acts of the taxpayer. Furthermore, it was immaterial, for present purposes, that when the sales were made the legal title was in the bank as trustee. As pointed out by the Board (R. 39), the conveyances were made to the bank for two purposes—first, to secure the bank for its loan then made to the taxpayer and for advances thereafter to be

made; and, second, to facilitate the execution and delivery of deeds to purchasers of the lots in the absence of the taxpayer. Nor is it of any particular import that the taxpayer's principal business was that of raising and selling farm produce. One may be engaged in several businesses at the same time.

The taxpayer relies upon the proposition that the properties sold in the three subdivision projects were acquired for the purpose of raising produce and that they could not have been held primarily for sale in the course of a subdivision business. If this case were controlled by the Revenue Act of 1921, such an argument would have some force. Section 206 (a) (6) of the Revenue Act of 1921, c. 136, 42 Stat. 227, did require that the property be "acquired and held * * * for profit or investment * * *", but all the subsequent revenue acts omitted the word "acquired." The purpose of the change made in the revenue act was to remove any doubt as to whether the statute referred to property held primarily for sale, whether or not it was included in inventory. See H. Rep. No. 179, 68th Cong., 1st Sess., p. 57.

In the recent case of *Roney v. Commissioner*, 67 F. (2d) 165 (C. C. A. 4th), certiorari denied, 290 U. S. 705, the court pointed out that, even though slight, the activities of the taxpayer were continuously carried on between the years 1922 and 1925, and concluded that (p. 166) "very slight activity constitutes 'doing business' when the end is profit."

In *Sloan v. Commissioner*, 63 F. (2d) 666, this Court said (p. 669):

As said by the Supreme Court in the case of *Flint v. Stone Tracy Co.*, 220 U. S. 107, 171, 31 S. Ct. 342, 357, 55 L. Ed. 389, Ann. Cas. 1912B, 1312: “ ‘Business’ is a very comprehensive term and embraces everything about which a person can be employed. Black’s Law Dict., 158, citing *People v. Commissioners of Taxes*, 23 N. Y. 242, 244. ‘That which occupies the time, attention, and labor of men for the purpose of a livelihood or profit.’ Bouvier’s Law Dict. [vol. 1], p. 273.”

In *Welch v. Commissioner*, 19 B. T. A. 394, affirmed *per curiam*, 59 F. (2d) 1085 (C. C. A. 6th), it was held that the subdivided property was held by the taxpayer primarily for sale in the course of his business although, due to ill health, he gave little personal attention to the developments, and though the lots were sold by many different real estate agents. In the more recent case of *Pope v. Commissioner*, 77 F. (2d) 599 (C. C. A. 6th), the court reversed the Board’s decision and allowed the treatment of the gain realized from the sale of lots as a capital gain. The following excerpt from the opinion clearly distinguishes such case from the one now before the court (p. 600):

It may be assumed that Miller and the Essex Company were engaged in the real-estate business, but the status of their profits is not in controversy. The question is whether a director and officer of a corporation, owning

a substantial amount of its stock but not active in its affairs, is engaged in the business in which the corporation is engaged.

The case of *Phipps v. Commissioner*, 54 F. (2d) 469 (C. C. A. 2d), is likewise distinguishable from the instant case. That the court there recognized the principles here urged is evidenced by the following excerpt from the opinion (p. 471):

There should be a greater continuity and larger absorption of time in such transactions to make the taxpayers more than investors. A fair reading of the record makes it clear that nothing was done during the years in question but to hold land for sale which had been previously purchased, and to accept such offers from purchasers as were presented by brokers and seemed satisfactory. There was during the years in question no activity amounting to a trade or business within the meaning of the statute, and whether there was such a trade or business depended on the situation of the taxpayers at the time of the sale. They had not continuously engaged in the development and sale, or the purchase and sale of lands.

It is submitted that the principles of law involved in cases of this type are clear. The decision in each instance must depend upon the particular facts before the court. *Von Baumbach v. Sargent Land Co.*, 242 U. S. 503. The sole question presented on this review is whether the evidence is legally sufficient to sustain the Board's finding that the lands were held by the taxpayer primarily for

sale in the course of his trade or business. *Phillips v. Commissioner*, 283 U. S. 589; *Pope v. Commissioner*, *supra*.

On page twenty-four of his brief, taxpayer contends that when the land itself was no longer valuable in his produce business, the disposition of it amounted to a liquidation, but to that extent only, conceding that he was not liquidating his produce business. The cases there cited do not fit this case. In this Court's decision in *Commissioner v. Atherton*, 50 F. (2d) 740, where the issue was whether the trust formed for the liquidation and distribution of real estate holdings of a transit company was a pure trust or an association taxable as a corporation, it was pointed out (p. 741) that "there was and is nothing that required the time, attention, or labor of any one for profit or for livelihood." There the land, in its existing condition, was listed with general land agents for sale. The trustees "did no business except to collect rent on the parcels involved, pay taxes and expenses thereon." Such a case is clearly distinguishable from the one at bar, where the lands held were not being sold as such but were, through the involved and continuous efforts of the taxpayer and his own agents, converted into a new type. The Board correctly found (R. 41) that "what he has done is to take certain assets individually owned and devoted them to a new purpose."

It is submitted that the evidence amply supported the Board's finding that the taxpayer was

engaged in the subdivision business during the years involved.

CONCLUSION

Since the lots were held by the taxpayer primarily for sale in the course of his business, the profits arising from the sale of those lots are not subject to the capital gain provisions of the statute. The decision of the Board of Tax Appeals should be affirmed.

Respectfully submitted.

FRANK J. WIDEMAN,
Assistant Attorney General.

SEWALL KEY,
JOSEPH M. JONES,
Special Assistants to the Attorney General.

NOVEMBER 1935.

No. 7843

15

United States

Circuit Court of Appeals

For the Ninth Circuit.

WILLIAM R. MACKLIN,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

Transcript of Record

Upon Appeal from the District Court of the United States
for the Western District of Washington,
Northern Division.

FILED

JUN 14 1935

PAUL H. O'BRIEN.

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[Clerk's Note: When deemed likely to be of an Important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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NAMES AND ADDRESSES OF COUNSEL.

MESSRS. WINTER S. MARTIN,

and

HARRY S. REDPATH,

605 Colman Building,

Seattle Washington,

MESSRS. LEWIS & CHURCH,

Port Angeles, Washington,

Attorneys for Appellant.

MESSRS. J. CHARLES DENNIS

and

GERALD SHUCKLIN,

222 Post Office Bldg.,

Seattle, Washington,

Attorneys for Appellee. [1]*

*Page numbering appearing at the foot of page of original certified Transcript of Record.

United States District Court, Western District of
Washington, Northern Division.

November Term, 1934

No. 43521

UNITED STATES OF AMERICA,

Plaintiff,

vs.

WILLIAM R. MACKLIN,

Defendant.

INDICTMENT

United States of America
Western District of Washington,
Northern Division—ss:

Violation Sections 404 and 1181, Title 26, U.S.C.A.

The grand jurors of the United States of America
being duly selected, impaneled, sworn, and charged
to inquire within and for the Northern Division of
the Western District of Washington, upon their
oaths present: [2]

COUNT I.

That WILLIAM R. MACKLIN, whose true Chris-
tian name is to the Grand Jurors unknown, on or
about the sixteenth day of July, in the year of Our
Lord one thousand nine hundred thirty-four, at the
City of Port Angeles, in the Northern Division of
the Western District of Washington, within the jur-
isdiction of this Court, and within the Internal Rev-

venue Collection District of Washington, then and there being, did then and there knowingly, wilfully, unlawfully and feloniously remove and aid and abet in the removal of approximately three (3) gallons of moonshine whiskey, on which the tax due the Government of the United States had not then and there been paid, to those certain premises located at Port Angeles, Washington, known as 424 East 11th Street, a place other than a bonded warehouse provided by law, and did then and there conceal, and aid in the concealment of the said moonshine whiskey so removed; contrary to the form of the statute in such case made and provided, and against the peace and dignity of the United States of America.

And the grand jurors aforesaid, upon their oaths aforesaid, do further present:

COUNT II.

That WILLIAM R. MACKLIN, whose true and full name is to the grand jurors unknown, on or about the sixteenth day of July, in the year of our Lord, one thousand nine hundred thirty-four, at the City of Port Angeles, in the Northern Division of the Western District of Washington, and within the jurisdiction of this Court, then and there being, [3] did then and there knowingly, wilfully, unlawfully and feloniously remove, deposit and conceal, with intent to defraud the United States of the internal revenue taxes due thereon as fixed by law, at those certain premises known as, to-wit: 424 East 11th Street, at the City of Port Angeles, Washington, to-wit: three (3) gallons of moonshine whiskey; con-

trary to the form of the statute in such case made and provided, and against the peace and dignity of the United States of America.

J. CHARLES DENNIS

United States Attorney

GERALD SHUCKLIN

Assistant United States Attorney

A True bill.

B. F. BLACKBURN

Foreman

J. CHARLES DENNIS

U. S. Attorney

[Endorsed]: Presented to the Court by the Foreman of the Grand Jury in open Court, in the presence of the Grand Jury, and FILED in the U. S. DISTRICT COURT Dec. 8, 1934.

EDGAR M. LAKIN

Clerk

By TRUMAN EGGER

Deputy [4]

[Title of Court and Cause.]

ARRAIGNMENT AND PLEA.

Now on this 10th day of December, 1934, Gerald Shucklin, Assistant United States District Attorney, appearing for the plaintiff and Winter S. Martin, Esq., appearing as counsel for the defendant, on request the personal recognizance of the defendant stands until the arrival of bond given before the

United States Commissioner at Port Angeles, arrives, which bond with the consent of the United States District Attorney may then stand as bail herein. Defendant William R. Macklin is arraigned and answers that his true name is William R. Macklin. He enters a plea of not guilty to the indictment, with leave to move or demur to the indictment. Said cause is to be placed on the assignment calendar.

Journal No. 22

Page 627. [5]

District Court of the United States, Western District
of Washington, Northern Division

No. 43521

UNITED STATES OF AMERICA,

Plaintiff,

vs.

WILLIAM R. MACKLIN

Defendant.

VERDICT

WE, THE JURY IN THE ABOVE-ENTITLED CAUSE, FIND the defendant WILLIAM R. MACKLIN is guilty as charged in Count I of the Indictment herein; and further find the defendant WILLIAM R. MACKLIN not guilty as charged in Count II of the Indictment herein.

CHAS. T. SKINNER

Foreman.

[Endorsed]: Filed Mar. 27, 1935. [6]

[Title of Court and Cause.]

TRIAL RESUMED

Now on this 27th day of March, 1935, Gerald Shucklin, Assistant United States District Attorney, appearing for the plaintiff and Winter S. Martin, Esq., appearing as counsel for the defendant, the jury returns into court at 10 A. M. with a sealed verdict which is as follows, to wit: "We, the jury in the above-entitled cause, find the defendant WILLIAM R. MACKLIN is guilty as charged in Count I of the Indictment herein; and further find the defendant WILLIAM R. MACKLIN not guilty as charged in Count II of the Indictment herein. Chas. T. Skinner, Foreman." All jurors, defendant and counsel are present. The verdict is received, read, acknowledged by the jury, and the jury polled at request of the defendant, each juror answering that the verdict as read is his verdict. The verdict is ordered filed and the jury is excused from the case. The defendant's counsel orally moves for arrest of judgment and for a new trial, and that sentence be deferred. Motions in writing are directed to be filed, and Monday, April 8, 1935, is set as a time for hearing the same, and for judgment and sentence. The defendant is permitted to go on his present recognizance.

Journal No. 22,

Page 851 [7]

[Title of Court and Cause.]

MOTION FOR NEW TRIAL.

Comes now the defendant Macklin and moves for a new trial upon the several grounds as follows, towit:

(1) The Court erred in denying defendant's motion for a directed verdict of acquittal at the close of the Government's case.

(2) The Court erred in denying a similar motion for directed verdict of acquittal at the close of the defendant's case for the reason that there was no competent evidence or evidence of any kind or description which showed that Macklin had not paid the tax due on said three gallons of liquor. That the failure to pay tax on the three gallons of liquor was the gist of the offence and it was the duty on the part of the Government to allege and prove this fact towit: That the tax had not been paid by Macklin.

(3) The Court erred in failing to give the instructions requested on the part of the defendant to which defendant duly excepted at the close of the trial.

(4) The comment by Prosecutor on the failure of the defendant to take the witness stand was prejudiced error which requires a new trial.

(5) The acquittal of Count Two must of itself discharge the defendant as a matter of law.

WINTER S. MARTIN

Attorney for Defendant.

Received a copy of the within Motion this 3 day of
Apr. 1935.

J. CHARLES DENNIS

Atty for Pltff.

[Endorsed]: Filed Apr. 3, 1935. [8]

[Title of Court and Cause.]

ORDER

Now on this 8th day of April, 1935, Gerald Shucklin, Assistant United States District Attorney, appearing for the plaintiff and Winter S. Martin, Esq., appearing as counsel for the defendant, this cause comes on for hearing on motion for new trial and sentence of the defendant, and the same is ordered continued over one week.

Journal No. 22

Page 878 [9]

[Title of Court and Cause.]

HEARING.

Now on this 15th day of April, 1935, Gerald Shucklin, Assistant United States District Attorney, appearing for the plaintiff and Winter S. Martin, Esq., appearing as counsel for the defendant, this cause comes on for hearing on motion for new trial. The same is argued by counsel for the defendant and the motion is denied. Exception is allowed.

Journal No. 22

Page 888. [10]

In the United States District Court for the Western
District of Washington, Northern Division.

No. 43521

UNITED STATES OF AMERICA,

Plaintiff,

vs.

WILLIAM R. MACKLIN,

Defendant.

SENTENCE.

Comes now on this 15th day of April, 1935, the said defendant, William R. Macklin, into open court for sentence, and being informed by the court of the charges herein against him and of his conviction of record herein, he is asked whether he has any legal cause to show why sentence should not be passed and judgment had against him and he nothing says save as he before hath said. Wherefore by reason of the law and the premises, it is considered, ordered, and adjudged by the court that the defendant is guilty of removing and aiding and abetting in the removal of certain whiskey on which the tax due the Government of the United States had not then and there been paid as charged in count 1 of the indictment in violation of Section 404, Title 26, U.S.C.A. and that he be punished by being committed to the custody of the Attorney General of the United States, or his authorized representative for imprisonment in the Clallam County Jail at Port Angeles, Washington, or in such other prison as may be hereafter provided

for the confinement of persons convicted of offenses against the laws of the United States, for the period of four (4) months; and that he pay a fine of \$500.00. And the defendant is hereby remanded into the custody of the United States Marshal to carry this sentence into execution.

The defendant's attorney, Mr. Martin, asks that the defendant be allowed his liberty for a few days on his present bond until steps are taken to perfect appeal herein. The request is granted and commitment is stayed for five days and the Court permits the defendant to remain at liberty under present bond, during that time the defendant either to take steps to perfect his appeal or surrender himself to custody if appeal is not taken within said time.

Judgment & Decree

Vol. 9, Page 180. [11]

[Title of Court and Cause.]

HEARING.

(Defendant released on bail)

Now on this 18th day of April, 1935, Gerald Shucklin, Assistant United States District Attorney, appearing for the plaintiff and Winter S. Martin, Esq., appearing as counsel for the defendant, the defendant, WILLIAM R. MACKLIN, having served and filed notice of appeal and grounds of appeal now appears in open court and orally moves for an entered order fixing appeal bond herein in the same

amount as fixed in bond for his appearance before this Court, to-wit, \$750.00, and with the same sureties, and it is so ordered if the bond is satisfactory to the United States District Attorney, upon the justification thereon.

Journal No. 22.

Page 896 [12]

[Title of Court and Cause.]

PROCEEDINGS

(Showing issuance of Copy of Notice of Appeal and Docket entries to Appellate Court.)

* * * * *

April 18, 1935 Issue Copy of Notice of Appeal and Copy of Docket entries to C. C. A.

* * * * *

Criminal Docket No. 25

Page 221. [13]

[Title of Court and Cause.]

DEFENDANT'S NOTICE OF APPEAL TO THE
UNITED STATES CIRCUIT COURT OF
APPEALS FOR THE 9TH CIRCUIT.

1. Name and Address of Appellant are:—

William R. Macklin, 535 West Fourth Street
Port Angeles, Washington.

2. Names and addresses of appellant's attorneys are:—

Winter S. Martin, 605 Colman Building,
Seattle, Wash.,

Harry S. Redpath, 605 Colman Building,
Seattle, Wash.,

Lewis & Church, Port Angeles, Washington.

3. Offense

The indictment was drawn in two counts.

COUNT ONE.

This count charged defendant with violating section 404 U.S.C.A. Title 26 in that the defendant at Port Angeles, Washington within the Northern Division of the Western District of Washington, on or about July 16th, 1934, did unlawfully and feloniously remove three gallons of moonshine whiskey, on which the tax due the Government of the United States had not then and there been paid, to those certain premises located at Port Angeles, Washington known as 424 East 11th street, a place other than a bonded warehouse provided by law, and did then and there conceal and aid in [14] the concealment of the said moonshine whiskey so removed, contrary to the form of the statute in such case made and provided.

See Section 404, Title 26 U.S.C.A. being R. S. 3296.

COUNT TWO.

This count charged the defendant with violating section 1181, Title 26, U.S.C.A. in that the defendant

at Port Angeles, Washington within the Northern Division of the Western District of Washington on or about July 16th, 1934, did unlawfully and feloniously remove and aid and abet in the removal of three gallons of moonshine whiskey on which the tax due the government of the United States had not then and there been paid, to the premises No. 424 East 11th Street a place other than a bonded warehouse provided by law and did then and there conceal said moonshine whiskey so removed contrary to the Statute in such case made and provided.

This section 1181 of Title 26 U.S.C.A. is Sec. 3450 of the Revised Statutes.

4. Date of Judgment

Defendant was convicted of count one and found not guilty of Count two. Judgment and sentence was entered April 15, 1935 by the Honorable John C. Bowen, United States District Judge.

5. Defendant was adjudged to serve four months in Clallam County Jail at Port Angeles, Washington or at any other institution selected by the Attorney General and authorized by law. Defendant was also fined \$500.00 (Five Hundred Dollars) and required to stand committed until paid.

6. Defendant was enlarged on bail pending taking and perfecting his appeal, and required to furnish his bond on appeal after filing notice of Appeal. Said defendant is now at large on bail.

I, the above named appellant hereby appeal to the United States Circuit Court of Appeals for the 9th

Circuit, from the judgment [15] above mentioned on the grounds set forth below.

WILLIAM R. MACKLIN

Appellant

Dated this 18th day of April, 1935.

GROUND'S OF APPEAL.

The Government produced and offered four witnesses, two of whom were the arresting officers who testified under oath that on the evening of July 16th 1934, they went upon the rear of the premises numbered 424 East 11th Street in the city of Port Angeles and arrested the defendant Macklin as he stepped out of his automobile. They found three one-gallon glass containers, each containing one-gallon of alcohol whiskey. There was no tax stamp, label, mark, brand, or any printed or written notice of any kind on each or any of the containers. There was nothing on each or any container to indicate whether a tax of any kind had been paid upon the container or its contents. The containers were plain white bottles without identifying mark of any kind thereon.

No evidence of any kind was offered by the Government as to the non-payment of the Revenue Tax due thereon to the United States. The Government rested its case. Defendant did not take the stand and offered no evidence of any kind. At the close of the Government's case in chief and again after defendant closed without taking the witness stand and without offering proof, defendant moved for a directed verdict of acquittal upon the ground that

there was not a scintilla of evidence to sustain the material allegation of the Indictment, that the tax on said three gallons of moonshine whiskey so unlawfully [16] removed had not been paid. There was nothing on said containers to indicate that the tax had not been paid. The court denied each motion to all of which defendant then and there duly excepted which exception was by the Court allowed and noted.

The cause was then submitted to the jury which subsequently returned a verdict of guilty on count one, and not guilty of count two.

Before the jury retired to consider the case, and immediately after the Court had charged the jury, defendant excepted to the refusal of the court to instruct the jury as requested which exceptions were allowed and noted. Defendant will extend this matter of error in the refusal to instruct, in defendants assignments of error on this appeal.

In addition to the error in denying defendant's motion for a directed verdict of acquittal and the court's refusal to instruct as requested, duly excepted to when denied, viz: on the ground that the non-payment of the Government tax is the gist of the offense described in Sec. 404 Title 26 U.S.C.A. and the entire absence of proof of non-payment of tax in the Government's case required an acquittal the finding of not guilty in count two is the legal equivalent of not guilty in count one because only one *signle* offense was charged in each of said counts and the gist of the offense in each count was identical viz: there was but one removal of spirits to the premises 424 East 11th Street, Port Angeles. There was one

arrest at which time three one-gallon containers full of alcohol whiskey was found. The gist of the offense of count one was the gist of the offense charged in count two. The counts were identical in this respect. The jury in finding defendant not guilty under count two of any intent to defraud the United States in the matter of the payment of the tax, by the act of removing said liquor to [17] the identical premises mentioned in count one must be held to have exonerated the defendant of guilt under count one. A felonious removal of said three gallons of non-tax paid liquor was the gist of each offense.

Dated at Seattle, April 18, 1935.

Respectfully submitted

WINTER S. MARTIN

Of Counsel

Attorney for Appellant

WILLIAM R. MACKLIN

Appellant.

Copy received April 18, 1935.

J. CHARLES DENNIS

U. S. Attorney

GERALD SHUCKLIN

Asst. U. S. Atty.

[Endorsed]: Filed Apr. 18, 1935. [18]

[Title of Court and Cause.]

ORDER.

It appearing to the undersigned trial judge that the appellant above named on the 18th day of April,

1935, filed with the Clerk of this court a notice of appeal in the above entitled cause,

NOW THEREFORE, in pursuance of the Rules of Practice and Procedure in Criminal Cases adopted by the Supreme Court of the United States on May 7, 1935.

IT IS ORDERED that the above named appellant or his attorney and the United States Attorney do appear before the undersigned trial judge on the 22nd day of April, 1935, at 10:00 o'clock a.m. at the City of Seattle, in the Court Room of said Court, for such directions as may be appropriate with respect to the preparation of the record on appeal, including directions for the purpose of making promptly available all necessary transcripts of testimony and proceedings; and as to the time for the filing of an assignment of the errors of which the appellant complains if the record on appeal is to be without a bill of exceptions; as to the preparation and filing of the bill of exceptions and the settlement of the same by the undersigned trial judge; as to the contents of the transcript of record on said appeal and as to the time for the filing of said record with the clerk's certificate in the United States Circuit Court of Appeals for the Ninth Circuit, and as to all other matters pertinent to said appeal.

It is further ordered that the clerk of this court do forthwith serve a certified copy of this notice by

mail on the appellant or his attorney and on the United States Attorney for this District.

Dated Seattle, April 18, 1935.

JOHN C. BOWEN
District Judge.

[Endorsed]: Filed Apr. 18, 1935. [19]

[Title of Court and Cause.]

BAIL BOND ON APPEAL

We, William R. Macklin, as principal, and E. E. Nichols and Mrs. William R. Macklin, as sureties, jointly and severally acknowledge ourselves indebted to the United States of America in the sum of seven hundred fifty dollars (\$750.00) to be levied of our own goods and chattels, lands and tenements, upon this condition:

WHEREAS, the said William R. Macklin has appealed from the judgment and sentence of the above entitled court in said above cause entered heretofore on the 15th day of March, 1935, to the United States Circuit Court of Appeals for the 9th Circuit,

Now, therefore, if the said William R. Macklin shall prosecute his appeal with effect and personally be and appear before the said District Court when required to do so from day to day and term to term thereafter until the determination of said appeal and shall abide by and perform any order or judgment which may be rendered therein in said cause by the

District Court and/or the Circuit Court of Appeals for the 9th Circuit and shall not depart this district without leave thereof then this obligation to be void; otherwise to remain in full [20] force and virtue.

WITNESS OUR HANDS AND SEALS THIS
19th DAY OF APRIL, 1934.

[Seal] WILLIAM R. MACKLIN

[Seal] E. E. NICHOLS

[Seal] MRS. WILLIAM R. MACKLIN

APPROVED THIS 20th day of April, 1935.

J. CHARLES DENNIS

United States Attorney

By GERALD SHUCKLIN,

Asst. U. S. Atty.

TAKEN AND APPROVED THIS 20th day of
April, 1935.

[Seal] JOHN C. BOWEN

United States District Judge

Approved

W. BRUMFIELD

U. S. Comm'r [21]

United States of America

Western District of Washington

Northern Division—ss.

MRS. WILLIAM R. MACKLIN, being individually sworn, and being a surety on the annexed recognizance, deposes and says: That she resides at Port Angeles, in the County of Clallam, State of Washing-

ton in the above described District; that she is a freeholder in the said County and State and is the owner in fee simple (and in her own sole and separate right) of Lot Twelve (12) in Block Seventy-four (74) of the Townsite of Port Angeles, Washington.

E. E. NICHOLS, being individually sworn, and being a surety on the annexed recognizance, deposes and says: That he is a widower and resides at Port Angeles, in the County of Clallam, State of Washington, in the above described District; that he is a freeholder in said County, State and District; and is the owner in fee simple of Lot Three (3) in Block Eighty-seven (87) of the Townsite of Port Angeles, Washington;

And each of these affiants being individually sworn for themselves, depose and say: That they are worth the sum of Seven Hundred and Fifty Dollars (\$750.00) over and above all just debts and liabilities, in property subject to execution and sale, and exclusive of exemption by law from levy and sale under execution, and that their property consists of the above described real estate.

MRS. WILLIAM R. MACKLIN
E. E. NICHOLS

Sworn to before me and subscribed in my presence
this 19th day of April, 1935.

[Seal] DEVILLO LEWIS

Notary Public in and for the State of Wash-
ington, residing at Port Angeles.

[Endorsed]: Filed Apr. 20, 1935. [22]

[Title of Court and Cause.]

PROCEEDINGS.

(Showing Lodging of Bill of Exceptions)

* * * * *

April 23, 1935, Lodged Deft's Bill of Exceptions.

* * * * *

(Criminal docket No. 25

Page 221.) [23]

[Title of Court and Cause.]

ORDER

Now on this 25th day of April, 1935, Gerald Shucklin, Assistant United States District Attorney, appearing for the plaintiff and Winter S. Martin, Esq., appearing as counsel for the defendant, the United States District Attorney not objecting request of counsel for the defendant for further time to settle bill of exceptions is granted and time is ordered extended until Monday, May 6, 1935.

Journal No. 22.

Page 909 [24]

[Title of Court and Cause.]

HEARING.

(Order Extending Time)

Now on this 6th day of May, 1935, Gerald Shucklin, Assistant United States District Attorney, ap-

pearing for the plaintiff and Winter S. Martin, Esq., and Mr. Redpath, appearing for the defendant, this cause comes on for settling bill of exceptions, directions re appeal record. Proposed amendments are filed. The bill of exceptions and proposed amendments are considered by the Court, the bill settled and signed.

On motion of the defendant an order is entered extending the November 1934 Term of Court for thirty days for all purposes pertaining to appeal. On motion of the defendant an order is entered granting thirty days from date to file record on appeal with the Clerk of the Appellate Court.

Journal No. 22,

Page No. 932 [25]

[Title of Court and Cause.]

ASSIGNMENT OF ERROR.

Comes now the defendant in the above cause and assigns the following errors to be presented in his appeal, to-wit:

I.

The Court erred in denying defendant's motion for a directed verdict of acquittal submitted

a. at the close of plaintiff's case;

b. at the close of all the evidence after defendant rested his case. See Bill of Exceptions P. 30.

II.

The Court erred in denying defendants requested instructions numbered one, two and three to which refusal defendant duly excepted which exceptions were allowed and noted. See Bill of Exceptions P. 36.

III.

The Court erred in overruling Defendant's motion for new trial and in arrest of judgment upon the grounds stated in the written motion to which denial by the Court, defendant duly excepted.

WHEREFORE, defendant prays that his appeal be granted.

DATED AT SEATTLE Washington, this 23rd day of April, 1935.

WINTER S. MARTIN

Of Counsel for Defendant.

Copy of these assignments rec'd this 23rd day of April, 1934.

J. CHARLES DENNIS

U. S. Attorney.

[Endorsed]: Filed Apr. 23, 1935. [26]

[Title of Court and Cause.]

BILL OF EXCEPTIONS

Be it remembered that the Grand Jurors of the United States of America being duly selected, im-

paneled, sworn and charged to inquire within and for the Northern Division of the Western District of Washington, upon their oaths presented on December 8th, 1934, an indictment in two counts charging the defendant William R. Macklin with having violated sections 404 and 1181 Title 26, U.S.C.A. That defendant William R. Macklin upon the 10th day of December, 1934, was arraigned in person before the above entitled court and then and there pleaded not guilty to each of the said counts in said indictment.

Be it further remembered that on the 26th day of March, 1935, this said cause came on for trial before the Honorable John C. Bowen, one of the judges of said court. A jury therein was duly sworn to try said cause.

The United States to maintain the issues on its part called as a witness, one,

CLYDE J. SHAW,

who being first duly sworn, testified under oath as follows, to wit:—

“That he was employed by the United States as an investigator in the Alcohol Tax Unit of the Bureau of Internal Revenue; that early in the evening of July 16, 1934, while so employed at Port Angeles, Washington, he was parked in an auto in the [27] vicinity of the alley in the rear of No. 424 East 11th Street in said Port Angeles. That Mr. C. J. Gibbs, an investigator in the employ of the Alcohol Tax Unit of the Bureau of Internal Revenue accompanied him in his automobile.

That the witness observed two automobiles, one following the other, to enter the alley back of the premises 424 East 11th Street. There was one man in each car. That the first car to enter the alley was a Buick. Defendant driving a 1933 Chevrolet followed the other car into the alley. That the driver of the Chevrolet, afterward ascertained to be the defendant Macklin, drove from the alley in the rear of 424 East 11th street into and upon the rear of the premises 424 East 11th Street. That he brought his car to a stop and had just stepped out of his car carrying a carton containing empty one-gallon jugs when the witness and his brother officer drove in back of the premises and came to a stop a few feet from the Macklin car. Witness and officer Gibbs jumped out of their car and immediately stepped over to the Macklin car. The witness looked into the car and saw cartons, and bottles which indicated to him that the driver of the car had liquor in the car. That he immediately placed said driver under arrest. He searched the Chevrolet auto and there found some five or six empty one-gallon jugs and three full one-gallon glass jugs containing alcohol whiskey.

That the Government at this point produced a one-gallon glass container which was full of what the witness said was alcohol whiskey. This one-gallon container bore no tax stamp, receipts, mark or label of any kind except the Exhibit mark placed thereon after defendant Macklin's arrest. The said three-one-gallon containers were made of white glass and when seized bore no identifying mark of any kind

thereon. There was no mark, tag, label, or anything upon the said container to indicate that the tax had or had not been paid on the contents. Neither the containers nor the cartons bore tax stamps or labels of any kind at the time of the arrest.

That witness asked Mr. Macklin whose liquor that was, and [28] Macklin said it was his. Witness asked Macklin what kind of liquor it was. Macklin replied that it was alcohol whiskey.

In addition to the one-gallon container offered in evidence, *wutbess testufued* that two other one-gallon bottles each full of the same kind of liquor were found in Macklin's auto, at the same time. Each container was without any label or tag, or other mark. That the witness said that the officers remained at No. 424 East 11th street with Mr. Macklin in their custody for about fifteen minutes. That they then placed Mr. Macklin in their auto and took him to the Clallam County Jail at Port Angeles. That at the sheriff's office at the jail, Mr. Macklin was searched and found to have \$326.00 in his possession.

The witness was asked by defendants attorneys in substance:

Q. When you were waiting in the vicinity of 424 East 11th Street, were you waiting for Mr. Macklin?

The witness answered

A. No.

Q. Then Mr. Macklin was not the man that you had under suspicion and he was not the man you were waiting for.

Witness replied in the negative. Asked by Mr. Martin of defense counsel why he followed the Macklin car witness replied that he was watching all cars that were passing in that vicinity for the reason that he had received information that liquor would be transported to the place in question and that when the two cars came along and entered the alley he thought it best to investigate them. When he drove into the alley witness followed for the purpose of finding out who they were. That before making the arrest as the witness approached the Macklin car he could see containers and one-gallon bottles in the car. Witness said that Macklin told them he used to work as a shingle weaver but couldn't do that kind of work any more."

The Government called as its next witness:

"C. J. GIBBS

who was duly sworn and upon his oath testified in substance to the same facts as testified to by witness C. J. Shaw with the exception that he stated that he and Shaw had been [29] with Macklin about one hours time in the rear of the premises of 424 East 11th Street, Port Angeles. He further testified that the three gallons of alcohol whiskey had been brought by him to Seattle, Washington and there turned over to custodian A. D. Sides of the Bureau of Internal Revenue Alcohol Tax Unit."

The Government then called

MR. A. D. SIDES

who being first duly sworn in the above cause upon his oath testified in substance :

“That he was employed by the United States as an investigator of the Alcohol Tax Unit of Internal Revenue. That the three gallons of Alcohol whiskey had been turned over to him as custodian by officers Shaw and Gibbs. He identified the exhibit as one of the three containers turned over to him and testified that these containers had been in his possession until turned over to M. S. Strubin his succeeding custodian. He testified that no marks, stamps, or labels had been upon any of the bottles other than the identification label placed thereon by the Bureau of Internal Revenue after the arrest of Macklin. He further testified over objection of Macklin’s counsel that the exhibit contained alcohol whiskey and that he had tested the same.”

“M. F. SBRUBIN

called as the last witness for the prosecution being first duly sworn in the above cause upon his oath said in substance :

“That he was an employee of the United States as an investigator in the Alcohol Tax Unit of the Bureau of Internal Revenue. That he had succeeded A. D. Sides as the custodian of property for the alcohol tax Unit of Internal Revenue and received the three containers from custodian A. D. Sides, had

given his receipt therefor, and had had the same in his custody up to the time of trial when the exhibit was produced in court.”

At the conclusions of the testimony of these four witnesses above mentioned, the Government rested its case in chief. Whereupon defendant by his counsel moved the court to instruct the [30] jury to return a verdict of not guilty for the reason that the failure to pay the Government tax upon the three gallons of moonshine liquor constituted the gist of the offense under each count of the indictment to wit: Section 404 and 1181 Title 26 U.S.C.A. That under section 266 of Title 26 U.S.C.A. viz:—

“All distilled spirits found in any cask or package containing five gallons or more, without having thereon each mark and stamp required therefor by law, shall be forfeited to the United States.”

Under five gallons in any one container a wholly different rule applies. Intoxicating liquor in any container under five gallons is presumed to have been tax paid and the burden in such cases is upon the United States to prove that the tax on the said container containing less than five gallons had not been paid.

That there was not a scintilla of evidence in the Government's case pertinent to the question whether the tax had or had not been paid. There was absolutely no evidence of the non-payment of the tax. There was in each count of the indictment a material

allegation to the effect that the said tax upon said three gallons of moonshine liquor had not then and there been paid together with the further allegation, that the purpose and intent on the part of the defendant was to defraud the United States of its revenue which it would have received if the tax had been paid. Said motion was denied by the Court to which rule of the court the defendant then and there duly excepted which exception was noted of record by said court.

That the defendant then and there declined to testify in person and declined to offer any testimony in his behalf. That the Government offered no further evidence after the defendant had rested its case. That thereupon defendant renewed his motion to instruct the jury to return a verdict of not guilty for the same reasons offered when a similar motion was made at the close of the Government's case in chief. The court denied the motion [31] made at the close of the testimony to which ruling of the court the defendant then and there duly excepted which exception was noted by the court. That after the argument of counsel the Honorable court charged the jury as follows:

INSTRUCTION No. 1

“In this case there is one defendant on trial on two counts of the indictment. In each of these counts the defendant has entered a plea of not guilty, which places upon the prosecution the burden of showing beyond a reasonable doubt

the truth of every material allegation of the accusation on which he is tried.

In this case you will consider each count of the indictment separately, and if you have a reasonable doubt under the evidence of any material allegation of the count of the indictment you are considering, it is your duty to acquit as to that count; if you have no such reasonable doubt concerning any such allegation, it is your duty to convict as to the allegation you are considering."

INSTRUCTION No. 2

A reasonable doubt is just such a doubt as the term implies; a doubt for which you can give a reason. Not speculative, imaginary, or conjectural. It is such a doubt as when experienced by a man of ordinary prudence, sensibility and decision, in determining an issue of like concern to himself as that before the jury to the defendant, would make him pause or hesitate in arriving at a conclusion. It may be a doubt which is created by a want of evidence or it may be by the evidence itself. A juror is satisfied beyond a reasonable doubt when he is convinced to a moral certainty of the guilt of the parties charged.

INSTRUCTION No. 3

The defendant William R. Macklin is charged with violating the internal revenue laws of the United States. Count I charges that the defendant on or about the 16th day of July, 1934,

at the city of Port Angeles, Washington, knowingly, wilfully, unlawfully and feloniously removed and aided and abetted in the removal of approximately three gallons of moonshine whiskey on which the tax due the government of the United States had not then and there been paid to premises located at 424 East 11th Street in that city when it is claimed these premises were other than a bonded warehouse provided by law, and that he then and there concealed and aided in the concealment of the moonshine whiskey so removed.

Count II charges that on the same date at the same place the defendant did knowingly, wilfully, unlawfully and feloniously remove, deposit and conceal approximately three gallons of moonshine whiskey with intent to defraud the United States of the Internal Revenue tax due thereon as fixed by law at the said premises known at 424 East 11th Street, Port Angeles, Washington. [32]

If you find that the acts alleged in the indictment have not been proved beyond a reasonable doubt, then it is your duty to find the defendant not guilty. However, if you find that the acts alleged in the indictment have been proved beyond a reasonable doubt, then it is your duty to find the defendant guilty.”

INSTRUCTION No. 4

“Intent is an ingredient of crime. It is psychologically impossible for you to enter into

the mind of the defendant and determine the intent with which he operated. You must, therefore, determine the motive, purpose and intent from the testimony which has been presented, and you will consider all of the circumstances disclosed by the witnesses as testified to bearing in mind that the law presumes that every man intends the legitimate consequences of his own acts. Wrongful acts, knowingly or intentionally committed, cannot be justified, on the ground of innocent intent. The color of the act determines the complexion of the intent.”

INSTRUCTION No. 5

“There are two kinds of evidence. Direct or positive, and circumstantial. Now, direct and positive testimony is that which a person observes or sees or which is susceptible of demonstration by the senses, and circumstantial evidence is proof of such facts and circumstances concerning the conduct of the parties which conclude or lead to a certain inevitable conclusion. Now, circumstantial evidence is legal and competent as a means of proving guilt in a criminal case, but the circumstances must be consistent with each other, consistent with the guilt of the parties charged; inconsistent with their innocence and inconsistent with every other reasonable hypothesis except that of guilt, and when circumstantial evidence is of that character, it is alone sufficient to convict. You will review all

the circumstances in the light of this instruction.”

INSTRUCTION No. 6

“I instruct you that every person charged with crime is presumed to be innocent until the jury is convinced of guilt by evidence beyond every reasonable doubt. This presumption of innocence attaches to every act and expressed thought of the accused and remains with him throughout the trial until the case is committed to you. And it continues into your deliberations in the jury room until the proof submitted upon the entire case convinces you of his guilt beyond every reasonable doubt.”

INSTRUCTION No. 7

“I instruct you that the failure to testify creates no inference of Guilt. The presumption of innocence requires this: The defendant is entitled to have the government prove its case by evidence which convinces the jury of the guilt of the accused beyond every reasonable doubt, independently of whether the accused takes the stand or not.” [33]

INSTRUCTION No. 8

“You are instructed that you are the sole and exclusive judges of the evidence in this case. You must determine what the facts in the case are. You are likewise the sole and exclusive judges of the credibility of the witnesses who

have testified before you, and in determining the weight or credit you desire to attach to the testimony of any witness, you will take into consideration the reasonableness of the story, the opportunity of the witnesses for knowing the things about which they have testified, the interest or lack of interest in a particular witness in the result of this trial; surround each witness with all the circumstances disclosed, all the testimony given here, and then determine who told the truth.”

INSTRUCTION No. 9

“The indictment in this case will be sent to the jury room with you merely to show you the paper charge against the defendant, but is not to be considered as evidence. You will take with you to the jury room the exhibit in the case. The verdict is in the usual form. Before the word “guilty” is a blank, and you will write in there “is” or “not” as you find. It will require your entire number to agree upon a verdict, and when you have agreed you will cause your verdict to be signed by your foreman, whom you will elect from among your number immediately upon retiring to the jury room.”

which said charge of the court above set forth comprised all of the instructions given to the jury in said cause. Defendant having duly presented at the opening of the trial three requested instructions now at the close of the court’s charge and while court was

in session and before the jury had retired from the jury box to consider said case, defendant in presence of the court and jury duly excepted to the refusal of the court to give defendant's requested instructions No. 1, 2, and 3 which were as follows towit:

INSTRUCTION No. 1

"I instruct that where less than five gallons of intoxicating liquor are found in any one container or vessel, and the said container, vessel or receptacle bears no revenue stamp thereupon showing the payment of tax, the law presumes that the tax was paid and it then becomes the duty of the government to prove beyond every reasonable doubt that the tax upon said liquor had not been paid. Proof of non-payment must appear in the case without regard to any stamp on the bottle, jug or container."

INSTRUCTION No. 2

"I instruct you to return a verdict of not guilty in this case for the reason that there is no evidence in this case that the tax on this liquor has not been paid." [34]

INSTRUCTION No. 3

"I instruct you that upon the Government's case which is now closed it is your duty to return a verdict of not guilty to each of the counts of this indictment. You will remain in your jury box and your foreman will sign the verdict of not guilty."

That the court then and there noted defendant's exception to its refusal to so instruct and allowed the same.

That the court then submitted said cause to the jury which after due deliberation returned its verdict of guilty as charged under Count one and not guilty of Count two. Verdict was entered on March 27, 1934. Thereupon on said day Defendant moved for a new trial and in arrest of Judgment in substance towit:

“That there was no evidence to support the allegations of the indictment that the tax had not been paid and that by reason thereof, motions for a directed verdict should have been granted.”

“That prejudicial error resulted from the Court's refusal to instruct as requested and that the finding of not guilty under Count two operated as a matter of law to discharge defendant under Count one notwithstanding the verdict.”

The court continued the hearing on motion for new trial until April 8th 1935 and upon April 8th 1935 again continued said cause until April 15th for hearing motion, and on said day denied same, and thereupon the Court imposed judgment and sentence of the Court which is of record in said cause.

The court after sentence considered the matter of bail pending appeal and ruling that it was a proper case for bail admitted defendant to bail.

And forasmuch as the evidence and proceedings and matters of exception above set forth do not fully

appear of record, the defendant by his attorney tenders this bill of exceptions and prays that the same be signed and sealed by the court here, pursuant to the statute in such case made and provided.

Which is done accordingly this 6th day of May, 1935.

JOHN C. BOWEN

Trial Judge

Copy of the Bill of Exceptions received this 23rd day of April 1935.

J. CHARLES DENNIS

Assistant U. S. Attorney

[Endorsed]: Filed Apr. 23, 1935. [35]

[Title of Court and Cause.]

PRAECIPE FOR APPELLATE RECORD.

TO THE CLERK OF THE ABOVE ENTITLED COURT:

You are hereby requested to take a transcript of record to be filed in the United States Court of Appeals for the 9th Circuit pursuant to an appeal taken and noticed in the above entitled cause and to include in such transcript of record the following papers and documents, to wit:—

1. Indictment.

2. Plea of Not Guilty December 10, 1934. Journal Record.

3. Verdict of jury acquitting defendant of count 2 and finding him guilty of count 1 as charged in the indictment.

4. Journal entry March 27 showing oral motion for new trial and arrest of judgment immediately upon return of verdict.

5. Written motion for new trial.

6. Journal entry continuing hearing on motion for new trial from April 8 to April 15.

7. April 15th motions for new trial and in arrest of judgment denied.

8. Judgment and sentence of the court April 15, 1935.

9. Journal entry fixing amount of appeal bond and enlarging defendant on bail.

10. Journal entry copy of notice of appeal and docket entries sent to San Francisco by Clerk of District Court. [36]

11. Notice of Appeal filed and served April 18th.

12. Clerk prepared Court order entered April 18 fixing April 22 re the time within which to prepare and file assignment of errors and to settle and allow bill of exceptions.

13. April 20, 1934 bail bond on appeal approved and filed.

14. Clerk's entry noting bill of exceptions lodged in clerk's office, April 23.

15. April 25 journal order continuing time to settle bill of Exceptions to May 6th.

16. Bill of Exceptions settled and signed.

17. Order extending time.

18. Order extending time to lodge record.

19. Copy of this praecipe.
20. Clerk's Certificate to record.

WINTER S. MARTIN

Of Counsel for Defendant

Copy of within praecipe received

J. CHARLES DENNIS

Attorney for plaintiff.

[Endorsed]: Filed May 10, 1935. [37]

[Title of Court and Cause.]

CERTIFICATE OF CLERK U. S. DISTRICT
COURT TO TRANSCRIPT OF RECORD ON
APPEAL.

United States of America,
Western District of Washington—ss:

I, EDGAR M. LAKIN, Clerk of the above entitled Court, do hereby certify that the foregoing typewritten transcript of record, consisting of pages numbered from 1 to 37 inclusive, is a full, true and complete copy of so much of the record, papers and other proceedings in the above and foregoing entitled cause, as the same remain of record and on file in my office, as is required by praecipe of counsel filed and shown herein, with the exception of the Bill of Exceptions and Assignments of Error, the originals of which are transmitted with this transcript; and that the foregoing constitute the record on appeal herein from the judgment of said United States Dis-

trict Court for the Western District of Washington to the United States Circuit Court of Appeals for the Ninth Circuit.

IN WITNESS WHEREOF I have hereunto set my hand and affixed the official seal of said District Court, at Seattle, in said District, this 20th day of May, 1935.

[Seal]

EDGAR M. LAKIN,

Clerk, United States District Court, Western
District of Washington,

By TRUMAN EGGER

Deputy. [38]

[Endorsed]: No. 7843. United States Circuit Court of Appeals for the Ninth Circuit. William R. Macklin, Appellant, vs. United States of America, Appellee. Transcript of Record. Upon Appeal from the District Court of the United States for the Western District of Washington, Northern Division.

Filed May 22, 1935.

PAUL P. O'BRIEN

Clerk of the United States Circuit Court of Appeals
for the Ninth Circuit.

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In the
United States Circuit Court
of Appeals
For the Ninth Circuit

No. 7843

WILLIAM R. MACKLIN,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

Appellant's Brief

*Upon Appeal from the District Court of the United
States for the Western District of Washington,
Northern Division*

LEWIS & CHURCH
Port Angeles, Washington

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WINTER S. MARTIN,
Of Counsel,

FILED

JUL 29 1935

PAUL R. GORDEN,

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In the
**United States Circuit Court
of Appeals**
For the Ninth Circuit

No. 7843

WILLIAM R. MACKLIN,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

Appellant's Brief

*Upon Appeal from the District Court of the United
States for the Western District of Washington,
Northern Division*

STATEMENT OF THE CASE

Defendant William R. Macklin was indicted at Seattle, December 8, 1934, for a violation of Sections 404 and 1186 of Title 26 U. S. C. A. It becomes important to study the language of the two counts of the indictment with relation to one of the assignments of error. Therefore we present the full text of the two counts omitting captions and merely formal parts.

Count I charged a violation of Section 404 of Title 26 U. S. C. A. (R. S. 3296).

COUNT I.

That WILLIAM R. MACKLIN, whose true Christian name is to the Grand Jurors unknown, on or about the sixteenth day of July, in the year of Our Lord one thousand nine hundred thirty-four, at the City of Port Angeles, in the Northern Division of the Western District of Washington, within the jurisdiction of this Court, and within the Internal Revenue Collection District of Washington, then and there being, did then and there knowingly, wilfully, unlawfully and feloniously remove and aid and abet in the removal of approximately three (3) gallons of moonshine whiskey, on which the tax due the Government of the United States had not then and there been paid, to those certain premises located at Port Angeles, Washington, known as 424 East 11th Street, a place other than a bonded warehouse provided by law, and did then and there conceal, and aid in the concealment of the said moonshine whiskey so removed; contrary to the form of the statute in such case made and provided, and against the peace and dignity of the United States of America.

Count II charged a violation of Section 1181 of Title 26 U. S. C. A. (R. S. 3450) (Tr. 3).

COUNT II.

That WILLIAM R. MACKLIN, whose true and full name is to the grand jurors unknown, on or about the sixteenth day of July, in the year of our Lord, one thousand nine hundred thirty-

four, at the City of Port Angeles, in the Northern Division of the Western District of Washington, and within the jurisdiction of this Court, then and there being, (3) did then and there knowingly, wilfully, unlawfully and feloniously remove, deposit and conceal, with intent to defraud the United States of the internal revenue taxes due thereon as fixed by law, at those certain premises known as, to-wit: 424 East 11th Street, at the City of Port Angeles, Washington, to-wit: three (3) gallons of moonshine whiskey; contrary to the form of the statute in such case made and provided, and against the peace and dignity of the United States of America.

See Tr. p.p. 2, 3, and 4.

Defendant Macklin entered a plea of "Not guilty" to each count. See Tr. p.p. 4 and 5.

The case was called for trial in the United States District Court at Seattle before the Honorable John W. Bowen and a jury on March 27, 1935. Later on said day the jury returned a verdict of guilty as charged in Count I, and not guilty as charged in Count II. Defendant's counsel upon the reading and entry of the verdict moved immediately in open court for a new trial and in arrest of judgment. Later within the time allowed therefor defendant served and filed his written motions. (Tr. 6-7).

The evidence at the trial showed that on July 16, 1934, Clyde J. Shaw and C. J. Gibbs, United States Revenue officers, in a parked automobile near the

alley in the rear of 424 East 11th Street, in Port Angeles, Washington, observed two automobiles, one following the other, to enter the alley at the rear of the said premises. The first car which entered the alley was driven upon the said premises, followed by the defendant Macklin who was driving a 1933 Chevrolet Automobile. These two officers in their parked car were watching for persons who they had reason to believe, were expected to pass them on the road in the vicinity of said alley. When they saw the two automobiles pass their car and enter the alley, they followed closely behind. As the two automobiles came to a stop at the premises of 424 East 11th Street, the officers jumped out of their car and caught Macklin as he was leaving his car carrying a carton containing empty one - gallon containers. They looked into the defendant's automobile and saw some other cartons and arrested him in the belief that he was violating the liquor laws. After they had placed him under arrest, they searched his car and found five or six empty one-gallon jugs each of which was made of white glass. They also found three full one-gallon glass jugs each containing whiskey. See Tr. 23-27. In support of these statements, Mr. Shaw produced and identified a one-gallon glass container which was full of what he said was alcohol whiskey. We quote from the Bill of Exceptions as follows:

“This one-gallon container bore no tax stamp receipts, mark or label of any kind except the Exhibit mark placed thereon after defendant Macklin’s arrest. The said three one-gallon containers were made of white glass and when seized bore no identifying mark of any kind thereon. There was no mark, tag, label, or anything upon the said container to indicate that the tax had or had not been paid on the contents. Neither the containers nor the cartons bore tax stamps or labels of any kind at the time of the arrest.” (Tr. 25.)

This officer testified that he asked Mr. Macklin, whose liquor it was and that Macklin answered that it was his. He then asked Macklin what kind of liquor it was and according to the officers statements, Macklin replied that it was alcohol whiskey. Mr. Shaw further testified that there were two other one-gallon containers each of which was full of the same kind of liquor. We quote again from the Bill of Exceptions:

“Each container was without any label or tag or other mark.” (Tr. 26.)

The witness was asked by defendant’s attorneys, in substance the following questions:

“Question: When you were waiting in the vicinity of 424 East 11th Street, were you waiting for Mr. Macklin?”

Witness answered “No.”

“Question: Then Mr. Macklin was not the man whom you suspected and he was not the man whom you were waiting for?”

Witness replied in the negative. (Tr. 26-27.)

Mr. Shaw stated further that he followed the Macklin car because he was watching all cars passing in the vicinity. That he had received information that liquor would be transported to the place in question and that when the two cars came along and entered the alley he thought it best to investigate.

C. J. Gibbs, the other Revenue officer who accompanied Mr. Shaw to the premises and made the arrest, testified in substance the same as his brother officer Shaw. (Tr. 27-28.)

Messrs. Shaw and Gibbs seized the three one-gallon containers and took the same to Seattle to use as evidence against Macklin.

The Government called two other witnesses, from its alcohol Tax Unit Division of the Bureau of Internal Revenue at Seattle, to testify that they had had the custody of seized liquor from the time it was delivered dence at the trial. They also testified that the three one-gallon jugs each of which was filled with liquor bore no stamp marks, tax labels or notices of any kind upon them, other than the identifying labels placed on the same by the Internal Revenue Bureau after Macklin's arrest. (Tr. 28-29.)

After the Government had rested its case in chief, defendant's counsel moved the court to instruct the

jury to return a verdict of "Not Guilty" upon each count for the reason that there was no evidence of any kind in the record to support the material allegation of each count of the indictment, to the effect that the tax due the United States on said liquor had not been paid.

That inasmuch as only three (3) gallons of liquor were found in Macklin's car, and as each gallon was contained in a one-gallon glass jug, which had no identifying mark label, stamp, or tag of any kind, there was nothing on the jugs which would bear upon the question of whether the tax had or had not been paid. And as there was not a *scintilla* of evidence in the case which in any manner pertained to the question of tax payment, the court should instruct the jury to return a verdict for the defendant. The tax is presumed to have been paid on liquor which is found in a container, jug or vessel of any kind of less than five gallons capacity. That in these circumstances the burden was upon the United States to prove beyond a reasonable doubt that the tax on said liquor had not been paid.

The Court overruled defendant's motion for a directed verdict, whereupon defendant excepted to the refusal of the Court to grant the said motion.

Defendant's counsel then stated to the Court that defendant would offer no evidence, and would decline

to testify in his own behalf. Thereupon defendant again moved for a directed verdict of not guilty upon the same grounds which he had urged in support of the first motion. The Court denied this second motion for a directed verdict to all of which defendant noted an exception.

Arguments of Counsel were then made after which the Court instructed the jury as to the law of the case.

Defendant had requested in writing that the Court give the following instructions, viz:

INSTRUCTION NO. 1.

“I instruct you that where less than five gallons of intoxicating liquor are found in any one container or vessel, and the said container, vessel or receptacle bears no revenue stamp thereupon showing the payment of tax, the law presumes that the tax was paid and it then becomes the duty of the government to prove beyond every reasonable doubt that the tax upon said liquor had not been paid. Proof of non-payment must appear in the case without regard to any stamp on the bottle, jug or container.

INSTRUCTION NO. II.

“I instruct you to return a verdict of not guilty in this case for the reason that there is no evidence in this case that the tax on this liquor has not been paid. (34)

INSTRUCTION NO. III.

“I instruct you that upon the Government's case which is now closed it is your duty to return a verdict of not guilty to each of the counts of

this indictment. You will remain in your jury box and your foreman will sign the verdict of not guilty."

That the court then and there noted defendant's exception to its refusal to so instruct and allowed the same. None of these requested instructions were given in the Court's instructions to the jury. (See Court's Instructions, p.p. 30-31.)

That the court then submitted said cause to the jury which after due deliberation returned its verdict of guilty as charged under Count I and not guilty under Count II. Verdict was entered on March 27, 1935. Thereupon on said day defendant moved for a new trial and in arrest of Judgment in substance, to-wit:

"That there was no evidence to support the allegations of the indictment that the tax had not been paid and that by reason thereof, motions for a directed verdict should have been granted."

"That prejudicial error resulted from the Court's refusal to instruct as requested and that the finding of not guilty under Count II operated as a matter of law to discharge defendant under Count I notwithstanding the verdict."
(Tr. p. 7.)

The Court continued the hearing on motion for new trial until April 8th, 1935, and upon said day, again continued said cause until April 15th for hearing the motion, and on said day denied same, and

thereupon the Court imposed judgment and sentence of the Court which is of record in said cause. (Tr. p. 9.)

The Court, after sentence, admitted defendant to bail, pending his appeal. (Tr. p. 10.)

THE POINTS RELIED UPON BY APPELLANT
FOR REVERSAL IN HIS NOTICE OF AP-
PEAL (Tr. p. 11) ARE, VIZ:

1. The government failed to offer any evidence in support of either of the counts of the indictment which tended to prove that the tax had not been paid. The case as a whole lacked any evidence of non-payment of the tax. Under Section 266 U. S. C. A., Title 26, (R. S. 3289)

“All distilled spirits found in any cask or package containing five gallons or more, without having thereon each mark and stamp required therefor by law, shall be forfeited to the United States.”

This forfeiture section above cited rests upon Sections 332 and 335 of Title 26 U. S. C. A., being respectively R. S. 3320 and 3323, which require all casks or packages of distilled spirits containing five gallons or more, to be marked, branded and stamped.

From these sections we note that marking, branding and stamping do not apply to containers, jugs, or

receptacles of less than five gallons capacity and hence the forfeiture provisions of Section 266, Title 26, U. S. C. A. (R. S. 3289) do not apply, hence there could be no conviction under either of Sections 404 and/or 1181 of Title 26, U. S. C. A., without proof of the non-payment of the tax. The liquor contained in any receptacle of under five gallons capacity is presumed to have been tax-paid and this presumption casts the burden upon the Government of proving that the liquor tax on less than five gallons in anyone container had not been paid. The motion for a directed verdict should have been granted.

2. The verdict of not guilty on Count II was in legal effect an acquittal of Count I because the same proof was required to support each of the two counts. These two points were urged in a motion in arrest and for a new trial which were by the Court, denied, to which defendant duly excepted.

SPECIFICATIONS OF ERROR (Tr. p. 22)

1. The Court erred in denying defendant's motion for a directed verdict of acquittal submitted

a. At the close of Government's case in chief, and

b. Again when defendant rested, which motions were identical and were based on the absolute failure to prove that the Government tax on said liquor contained in three one-gallon jugs had not been paid.

That defendant then and there noted an exception to the Court's refusal to grant said motion in each instance.

2. The Court erred in refusing to give defendant's requested instructions numbered I to III inclusive, viz:

INSTRUCTION NO. I.

"I instruct you that where less than five gallons of intoxicating liquor are found in any one container or vessel, and the said container, vessel or receptacle bears no revenue stamp thereupon showing the payment of tax, the law presumes that the tax was paid and it then becomes the duty of the government to prove beyond every reasonable doubt that the tax upon said liquor had not been paid. Proof of non-payment must appear in the case without regard to any stamp on the bottle, jug or container."

INSTRUCTION NO. II.

"I instruct you to return a verdict of not guilty in this case for the reason that there is no evidence in this case that the tax on this liquor has not been paid. (34)

INSTRUCTION NO. III.

"I instruct you that upon the Government's case which is now closed it is your duty to return a verdict of not guilty to each of the counts of this indictment. You will remain in your jury box and your foreman will sign the verdict of not guilty."

3. The Court erred in denying defendant's motion for a new trial and in arrest of judgment particularly

on the principal ground that the verdict of the jury in acquitting the defendant on Count II operated as a matter of law to acquit the defendant of Count I because the identical proof required to support Count II was likewise required to support Count I. The crimes charged in the two counts were the same with slight differences in phraseology, and the proof required to support each of the counts was identical as to time, place, person and subject matter. The gist of one was the gist of the other.

ARGUMENT

I. THE MOTIONS FOR A DIRECTED VERDICT OF NOT GUILTY

These motions should have been granted. The failure to direct a verdict of acquittal duly excepted to was reversible error.

The Federal Statutes require spiritous liquor to be marked, branded and stamped with a revenue stamp. This duty is imposed upon a United States Gauger whenever the cask or package contains more than five gallons by Section 332 U. S. C. A., Title 26 (R. S. 3320). Under Section 335 U. S. C. A., Title 26 (R. S. 3323) the law requires every package of spirits filled on the premises of a wholesale liquor dealer

which contains more than five gallons on which the dealer has paid the tax, to be branded, marked and stamped. Non-compliance on the part of the Gauger or Wholesaler is penalized.

It thus appears that all spiritous liquor contained in a receptacle of five gallons capacity or more must be stamped, branded, marked and labeled as required by law; whereas there is no provision of the law with respect to liquor which is contained in a receptacle of less than five gallon capacity. In the case of a receptacle containing five gallons or more, the absence of the gauge mark and tax stamp shows that the legal requirements as to marking and stamping have not been observed. Hence the courts have said that in the event a cask, package or receptacle containing five gallons or more of spirits is not stamped and branded as required by law, there is a *prima facie* case of failure to pay the revenue duty upon said spirits. The burden is then upon the owner or possessor to show that the tax had been paid.

A container or receptacle of less than five gallons capacity and which has no revenue stamp upon it, raises no presumption re the payment of the tax. In these circumstances the burden is upon the Government to

prove non-payment of the tax like any other material allegation of the Indictment.

In fact the non-payment of the tax on the spirits involved in these two counts was the most essential element of the several elements of the offenses charged in the two counts, if indeed there were two distinct offenses charged.

There was a total and complete failure of proof as to the payment or non-payment of the tax due on the liquor mentioned in each count of the indictment. Only three gallons were involved and each gallon was contained within a one-gallon glass jug. Hence, there was no presumption as in the case of a five-gallon or larger container.

Three decisions of the Circuit Court of Appeals support this assertion, and none has been found to the contrary. See *Dukes vs. U. S.*, 275 Fed. 142 (4th C. C. A.). In that case officers went to the residence of the accused and found about three gallons of corn liquor. One of the arresting officers said that he was acquainted with "Blockade Liquor" and that in his opinion the liquor found on defendant's premises was "*Blockade Liquor*". No stamps or marks of any kind were found on the bottles or containers. We quote from the opinion:

"A package or cask of less capacity than five wine gallons containing distilled spirits was not

required by law to have upon it any stamps, marks, or brands denoting the payment of the tax on the contents. The following sections of the Internal Revenue Laws will throw light upon this subject:

“Sec. No. 3289. All distilled spirits found in any cask or package containing five gallons or more, without having thereon each mark and stamp required therefor by law, shall be forfeited to the United States.’ Comp. St. 6030.”

Section 3320, as amended by the act of July 16, 1892 and as further amended by the act of August 27, 1894 (Comp. St. p. 6102), is in part as follows:

“Whenever any cask or package, containing five wine gallons or more, is filled for shipment, sale, or delivery on the premises of any rectifier who has paid the special tax required by law, it shall be inspected and gauged by a United States gauger whose duty it shall be to mark and brand the same and place thereon an engraved stamp, which shall state the date when affixed and the number of proof gallons, and shall be in such form as shall be prescribed by the Commissioner of Internal Revenue with the approval of the Secretary of the Treasury.”

Section 3323, R. S., as amended by the act of July 16, 1892 (27 Stat. 200, Comp. St. p. 6104), provides that:

“Every package of distilled spirits containing five wine gallons or more, filled on the premises of a wholesale liquor dealer, who has paid the special tax required by law, shall

be marked, branded and stamped by such wholesale liquor dealer, in such manner and under such rules and regulations as the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, may prescribe."

"Taking these sections in connection with the other provisions of the law, and the regulations governing the stamping of original casks and packages of distilled spirits, to the end that they might be removed from the distillery warehouse or the general bonded warehouse in which they were stored, it will be observed, as we have stated above, that no cask or package of less capacity than five wine gallons, containing distilled spirits, required the presence upon it of stamps, marks, or brands to denote the payment of the tax on the contents. The retail liquor dealer was the instrumentality through which distilled spirits, in packages, casks, or vessels holding less than five wine gallons, were distributed to the public for consumption.

In contemplation of law, the retail dealer bought his stock of distilled spirits from distillers, wholesale liquor dealers, or rectifiers, and the spirits were bought in barrels, casks, or packages, bearing the stamps, marks, and brands to evidence the payment of the tax. From these containers the retail dealer dealt out distilled spirits to purchasers in quantities of less than five gallons, as before stated. The law protected the spirits sold by the retailer from seizure or confiscation, unless it was shown that it had been taken from an untaxpaid package. Therefore when distilled spirits were found in a vessel of less capacity than five wine gallons, the law presumed that it was taxpaid, and the burden was upon the party alleging the contrary to prove it,

and in a criminal case to prove it to the satisfaction of a jury beyond a reasonable doubt.

The nonpayment of the tax is an essential element (now Section 404 of Title 26, U. S. C. A.) of the offense denounced in Section 3296, and the burden was upon the government in this case to prove that fact beyond a reasonable doubt, in order to warrant a verdict of conviction. The witness Lockhart testified that he was acquainted with blockade whiskey, and that in his opinion that found in the possession of the defendant was of such character. He did not testify that the species of distilled spirits known as 'Blockade' differed from that on which the tax had been paid in color, flavor, odor, or in any other respect. We do not think that this evidence was sufficient to prove the fact that the distilled spirits found in defendant's possession was illicit." (The italics referring to U. S. C. A. are inserted by ourselves.)

Hester vs. United States (C. C. A. 4th Circuit), 284 Fed. 487. The facts were similar to those of the *Dukes* case. There the amount of liquor found in the possession of the accused was less than five gallons. Defense moved for a directed verdict because of failure of proof to show that the liquor tax on the particular spirits had not been paid. Motion denied and verdict of guilty rendered. As in the *Dukes* case the Government officers testified that the liquor in question was "new corn liquor" "untax-paid liquor—blockade liquor".

Referring to this testimony the Court said:

“This will not suffice to show whether, in dealing with a package of whiskey containing less than five gallons, it was in point of fact tax paid or not. The mere fact that it was new corn whiskey would not show that the tax had not been paid as, perchance it might have come from a registered distillery and bonded warehouse. In this case the spirits covered by the indictment consisted of less than five gallons, namely, a quart, and the defendant is entitled to the benefit of the presumption that the tax had been paid. *The burden was upon the Government to show to the contrary.* If the quantity had been greater than five gallons, the absence of stamps showing payment of the tax would place upon the accused the burden of showing that the tax had been paid. It was incumbent upon the government, in the circumstances of this case, where the tax on the spirits was presumed to have been paid, to establish the contrary by proof to the satisfaction of the jury beyond a reasonable doubt, which we think it utterly failed to do, and hence that the defendant’s motion to instruct a verdict in his behalf, should have been sustained. The case, it seems to us, falls strictly within the decision of this court in *Dukes vs. United States*, 275 Fed. 142, where the very question of the sufficiency of the proof of nonpayment of the tax, based upon mere observation of the spirits by witnesses, was involved. The court in that case held, as we hold here, that certainly in a prosecution under this section of the law, where nonpayment of the tax is the essence of the offense, the proof clearly failed to establish such nonpayment, and hence in this case there should be a reversal of the decision of the lower court.” *Reversed. (Italics ours.)*

Mickle vs. United States, 33 Fed. (2d) 684 (C. C. A. 8th). In this case there were six gallons of liquor. The liquor was contained in twelve one-half gallon jars. There was no label, stamp or mark on the jars. Prosecution was based on Section 404 of Title 26, U. S. C. A. (R. S. 3926).

“The fact that the half-gallon glass jars which the appellant had in his possession did not have on them internal revenue stamps was not sufficient to raise a presumption that the tax had not been paid and shift the burden of proof as to that element of the crimes charged from the government to the appellant. *Dukes vs. United States* (C. C. A. 4th), 275 F. 142, 146; *Hester vs. United States* (C. C. A. 4th), 284 F. 487, 488.

Prior to national prohibition it was entirely lawful to have in one's possession and to transport distilled spirits of less than five gallons in a container bearing no stamps. No provision of the law required stamps to be affixed to containers of less than five gallons of distilled spirits. See Sections 266, 332, 335, Title 26, U. S. C. A.”

This quoted excerpt which refers to the period before the 18th Amendment became effective, is equally applicable to the present time, now that it has been repealed. So far as the laws of the United States are concerned the possession of liquor in containers of less than five gallons is not unlawful unless the Revenue Tax upon the same has not been paid. If the tax has been paid the liquor becomes entirely lawful. We again quote from the *Mickle vs. U. S.*, *supra*:

“The fact that in this case the appellant had in his possession more than five gallons of whisky does not affect the situation, since he did not have any one container of more than five gallons. The presumption that the tax has not been paid only arises from the absence of stamps from a container having in it more than five gallons.

Nothing was proved against the appellant except possession and transportation of intoxicating liquor, offenses under the National Prohibition Act for which he might have been prosecuted and of which upon the record here he was clearly guilty. It was entirely within the rights of the appellee to proceed against him under the internal revenue laws, with their heavier penalties, but it then had a heavier burden of proof which here it did not sustain. The appellant was entitled to a directed verdict of not guilty.”

These cases establish the contention of appellant that his motion for a directed verdict upon each count of the indictment should have been granted.

II. THE VERDICT OF THE JURY ACQUITTING DEFENDANT OF COUNT II MUST AS A MATTER OF LAW OPERATE TO DIS- CHARGE DEFENDANT UPON COUNT I

Although the two counts were alleged to be under different sections—*i. e.*, Count I charging a violation of 26 U. S. C. A., Section 404, while Count II charged a violation of Section 1181 of Title 26.

We now set these sections out in parallel columns, viz:

Section 404.

Whenever any person removes, or aids or abets in the removal of any distilled spirits on which the tax has not been paid, to a place other than the bonded warehouse provided by law, or conceals or aids in the concealment of any spirits so removed, or removes, or aids or abets in the removal of any distilled spirits from any distillery warehouse, or other warehouse for distilled spirits authorized by law, in any manner other than is provided by law, or conceals or aids in the concealment of any spirits so removed he shall be liable to a penalty of double the tax imposed on such distilled spirits so removed or concealed, and shall be fined not less than \$200 nor more than \$5,000, and imprisoned not less than three months nor more than three years. (R. S. Sec. 3296: Mar. 3, 1877, c. 114 Sec. 1, 2, 19, Stat. 393; Aug. 27, 1894, c. 349, Sec. 52, 28 Stat. 565).

Section 1181.

This section deals primarily with forfeiture of goods or commodities and also in forfeiture of instruments of carriage or removal.

The pertinent parts of this statute insofar as they relate to the offense of the person violating the act are, to-wit:

* * * And every person who removes, deposits, or conceals, or is concerned in removing, depositing, or concealing any goods or commodities for or in respect whereof any tax is or shall be imposed, with intent to defraud the United States of such tax or any part thereof, shall be liable to a fine or penalty of not more than \$500.00. (R. S. Sec. 3450).

Each count charged the offense as committed on July 16, 1934, at Port Angeles. Each states that William R. Macklin did then and there within the Division and District aforesaid knowingly, wilfully, unlawfully, and feloniously,—

Count I

* * * “remove and aid and abet in the removal of approximately three gallons of moonshine whiskey, on which the tax due the Government of the United States had not then and there been paid, to those certain premises located at Port Angeles, Washington, known as 424 East 11th Street, a place other than a bonded warehouse provided by law and did then and there conceal and aid in the concealment of the said moonshine whiskey so removed contrary to the form of the Statutes, etc.”

* * *

Count II

* * * “remove, deposit and conceal, with intent to defraud the United States of the Internal Revenue taxes due thereon as fixed by law at those certain premises known as 424 East 11th Street at the City of Port Angeles, Washington, to-wit: three gallons of moonshine whiskey contrary to the form of the statute, etc.”

Let us note the points of identity and similarity in the counts. Each offense was alleged to have been committed on July 16, 1934, at Port Angeles, Washington, within the Court's Jurisdiction. Each was confined to one person, William R. Macklin. Each charged a *removal* of three gallons of moonshine

whiskey to the identical premises, 424 East 11th street. So far there is absolute identity. Count I charges that Macklin aided and abetted a removal but the proof was the same under each count. Macklin was the sole and only person involved in the transaction. He was alone. The proof wholly failed to connect the first car and its driver who drove into the alley with Macklin. The government officers offered no testimony as to who the driver was nor as to his mission in the alley or his purpose or reason in going upon the premises. There is absolutely no connection between the driver of the first car, or any other person at the premises, 424 East 11th, and Macklin. So far as that person is concerned he acted lawfully in every way in going into or upon the premises at East 11th Street.

This eliminates the allegation that Mr. Macklin was aiding and abetting some other person in the removal of the whiskey charged in Count I. The proof showed that he had no help or aid from any other person, at least so far as the record goes.

Each of the counts charges concealment as well as removal. In Count II the word "Conceal" is coupled with the words "removed", and "deposit" whereas in Count I the allegation is that defendant took the liquor to a place other than a bonded warehouse "*and*

*did then and there conceal * * * said moonshine whiskey so removed*". The only noticeable difference between the allegations of Count I and Count II is that the premises, 424 East 11th Street, are charged in Count I to be a "*place other than a bonded warehouse*": whereas in Count II the charge is that he removed, deposited and concealed three gallons of moonshine liquor at the "premises known as 424 East 11th Street". There may be some slight technical difference between the counts in this respect. The only other difference is that Count II has the charge "deposit" whereas there is no such term in Count I. In all other respects the counts are the same.

There was, however, but one transaction involved in the two counts of the Indictment. The charge of concealment in each count must be disregarded because there was no evidence of any concealment at the premises, No. 424 East 11th Street. The concealment is not predicated upon having the liquor in the car. The specific charge in each count is that the liquor was concealed at the premises, 424 East 11th Street. Defendant was arrested the moment after stepping from his automobile. He had no chance to conceal the liquor or make any other disposition of it, even if such had been his purpose and intention. Therefore, the only remaining elements of the of-

fense in each count are that he removed three gallons of moonshine whiskey upon which the tax had not been paid to 424 East 11th Street. Thus, we see clearly that there was only one transaction shown by the proof under both counts. The proof necessary to support Count II was necessary to support Count I. In fact there was no evidence in the case to show that the premises 424 East 11th Street was not a bonded warehouse. Nothing was said about whether the said premises were bonded or not bonded. The gist of each count was the removal of three gallons of moonshine whiskey to said premises without having paid to the United States the tax thereon. Therefore, the finding of not guilty under Count ~~II~~ was the legal equivalent to a specific finding that Macklin did not "remove, deposit and conceal" three gallons of moonshine whiskey at the premises, 424 East 11th Street, Port Angeles, with intent to defraud the United States of the Internal Revenue tax due thereon as fixed by law.

The Judges of the C. C. A. for the 3rd circuit in *Hohenadel Brewing Co. vs. U. S.*, 295 Fed. 489, at page 490, held that a verdict on the 7th Count of the Indictment had to find support on evidence different from the evidence offered in support of the first six counts upon which the verdict was "Not Guilty." We quote from the opinion, viz:

“If the government relies upon the facts charged in the other counts to sustain the verdict of guilty on the seventh count, the judgment cannot stand, for the jury has found as a fact that the company did not commit the acts therein charged and in that case the verdict, as defendant contends, would be ‘inexplicable and inconsistent’. Facts that have no legal existence may not support a verdict. *The verdict of guilty on the 7th count must be based on evidence other than that pleaded in support of the first six counts.* Is there such evidence?” Defendant was found guilty of making illegal sales of beer on specific dates in six counts. The jury returned a verdict of guilty on the 7th count.” (The italics are ours.)

Another case which clearly states this principle is *Rosenthal vs. United States*, 276 Fed. 714 (9th C. C. A., 1921) in which Judge Ross wrote the opinion. The facts are almost parallel to the case at bar.

The defendant was charged in the first count with having bought and received 39 cases of certain described cigarettes which had theretofore been stolen from a Southern Pacific freight train, while moving in Interstate Commerce well knowing that the cigarettes had been stolen. The second count charged the defendant with having the same cigarettes in his possession. The jury returned a verdict of not guilty as to Count I but guilty as to Count II. Judge Ross speaking for this court said:

"The difficulty is that there was but one transaction involved in the two counts of the indictment, which was based upon the statute mentioned, and, according to the evidence one transaction between the plaintiff in error and the thieves. By its verdict upon the first count of the indictment, the jury found that the plaintiff in error neither bought nor received the cigarettes from them with knowledge of the theft and by its verdict upon the second count that the plaintiff in error was at the same time and place in possession of the property with such guilty knowledge. The two findings were thus wholly inconsistent and conflicting. For this reason we feel obliged to reverse the judgment and remand the case for a new trial."

See *Morgan vs. Devine*, 237 U. S. 632 * * * 59 L. Ed. 1153, Sections 1052, 1062, Bishop's Criminal Law 8th Ed. Judgment reversed and case remanded for a new trial." We quote the Supreme Court:

"The test is whether, if what is set out in the second indictment had been proved under the first, there could have been a conviction; when there could, the second cannot be maintained; when there could not, it can be. Sec. 1052 Bishop's Criminal Law.

"As to the contention of double jeopardy upon which the petition of habeas corpus is rested in this case, this court has settled that the test of identity of offenses is whether the same evidence is required to sustain them; if not, then the fact that both charges relate to and grow out of one transaction does not make a single offense where two are defined by the statutes. Without repeating the discussion, we need but refer to *Carter v. McClaughry*, 183 U. S. 365, 46 L. Ed. 236, 22

Sup. Ct. Rep. 181; *Burton v. United States*, 202 U. S. 344, 377, 50 L. Ed. 1057, 1069, 26 Sup. Ct. Rep. 688, 6 Ann. Cas. 362, and the recent case of *Gavieres v. United States*, 220 U. S. 338, 55 L. Ed. 489, 31 Sup. Ct. Rep. 421."

We need only ask whether the same proof was required to support Mr. Macklin's conviction under Count I as was submitted under Count II. The Government had to prove under Count I that the "three gallons of moonshine" was not tax paid liquor. It had to prove that Macklin removed the non-tax liquor to the premises 424 East 11th Street. It had to prove the identical transaction of Count II in order to convict under Count I. Hence, the acquittal under Count II is a bar to a further prosecution under Count I. The motion in arrest should have been granted. The error is apparent on the face of the record and was subject to dismissal under the motion in arrest. It would serve only to delay and put the defense to further expense only to meet the same contention based upon double jeopardy.

Respectfully submitted,

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Of Counsel,



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IN THE
UNITED STATES CIRCUIT
COURT OF APPEALS
FOR THE NINTH CIRCUIT

No. 7843

WILLIAM R. MACKLIN,

Appellant,

vs.

UNITED STATES OF AMERICA,

Appellee.

Upon Appeal from the District Court of the United States for the
Western District of Washington, Northern Division

HONORABLE JOHN C. BOWEN, *Judge*

BRIEF OF APPELLEE

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PAUL B. O'BRIEN,

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BRIEF OF APPELLEE

STATEMENT OF THE CASE

William R. Macklin was indicted for violation of
Sections 404 and 1181 of Title 26, U.S.C.A. After a

presentation of the case the jury returned a verdict of guilty as charged in Count 1, being a violation of Section 404, and not guilty as charged in Count II which alleged a violation of Section 1181.

Clyde J. Shaw, Investigator of the Alcohol Tax Unit of the Internal Revenue Department, testified, together with C. J. Gibbs, another officer in the same employ, that on July 16, 1934, they were parked in an auto at Port Angeles, Washington, in the vicinity of the alley in the rear of Number 424 East 11th Street in the said city. At that time they were watching all cars which were passing in that vicinity for the reason that information had been received that liquor would be transported to the premises above. Shaw observed two automobiles, one following the other, entering the alley in back of Number 424 East 11th Street. There was one man in each car, the first car being a Buick, and the defendant followed, driving a 1933 Chevrolet. Macklin brought his car to a stop and had just stepped out of the car carrying a carton containing empty one-gallon jugs when Shaw and Gibbs drove in back of the premises and came to a stop a few feet from the Macklin car. Shaw and Gibbs saw the cartons and bottles which indicated to them that Macklin had liquor in the car. Macklin was placed under arrest and a search of the automobile disclosed five or six

empty one-gallon jugs and three full one-gallon jugs containing alcohol whiskey. (Tr. 24-25).

Shaw testified, as did Gibbs, that neither the containers nor the cartons bore tax stamps or labels of any kind at the time of the arrest. Macklin admitted to the officers that the liquor was his and that it was alcohol whiskey. Macklin was searched and was found to have \$326 in his possession. He told the officers that he used to work as a shingle weaver but couldn't do that kind of work any more. (Tr. 24-25).

ARGUMENT

QUESTIONS TO BE DETERMINED

Appellant's brief sets forth two points for answer which will be the scope of appellee's brief:

(1.) Was there sufficient evidence to prove the element of non-payment of tax in violation of Title 26, U.S.C.A., Section 404?

(2.) Did the acquittal of the violation of Title 26, U.S.C.A., Section 1181, bar conviction for violation of Title 26, U.S.C.A., Section 404, and was verdict inconsistent?

THERE WAS SUFFICIENT PROOF OF NON-PAYMENT OF TAX IN VIOLATION OF TITLE 26 U.S.C.A., SECTION 404.

Appellant has adopted a position which is cer-

tainly not tenable when considered in relation to the Liquor Taxing Act of 1934 (Title 26 U.S.C.A., Sections 267 to 273). This act requires that all containers of distilled spirits must have affixed thereto tax stamps, with certain exceptions not important here. This was in effect when the crime was committed on July 16, 1934. (Tr. 25-26). The act completely nullifies the section cited by appellant which required that all containers of five gallons or more must bear upon them stamps denoting payment of tax. So cases cited based upon that statute can be of no efficacy now, except to extend the doctrine of presumption to all containers of distilled spirits. Whereas, prior to the passage of the Liquor Taxing Act of 1934 such a position might have weight, such is not the case now. The logical conclusion is that the cases cited by appellant should be extended now in their presumption from five-gallon containers or more to include containers of less capacity. The pertinent provisions of Section 267, Title 26, U.S.C.A. (Liquor Taxing Act of 1934) are as follows:

“No person shall * * * transport, possess, buy, sell, or transfer any distilled spirits, unless the immediate container thereof has affixed thereto a stamp denoting the quantity of distilled spirits contained therein and evidencing payment of all internal-revenue taxes imposed on such spirits.

* * *” (Jan. 11, 1934, c.1, Title II, Sec. 201, 48 Stat. 316.)

The pertinent provisions of Section 272, Title 26, U.S.C.A. (Liquor Taxing Act of 1934) are as follows:

“All distilled spirits found in any container required to bear a stamp by sections 267 to 273 of this title, which container is not stamped in compliance therewith and regulations issued thereunder, shall be forfeited to the United States.

* * *” (Jan. 11, 1934, c.1, Title II, Sec. 206, 48 Stat. 317.)

It will be noted in reading the latter section that this completely supersedes Section 266, Title 26, U.S. C.A., which provided as follows:

“All distilled spirits found in any cask or package containing five gallons or more, without having thereon each mark and stamp required therefor by law, shall be forfeited to the United States.”

Instructions given by the Court to the jury provided that the government had to prove beyond a reasonable doubt the allegations set forth in the two counts of the indictment. (Tr. 30-35). The Court did not instruct that the jury could presume from the fact that there were no tax stamps on the containers that the tax was unpaid, and then the burden of proving that the tax was paid would shift to the defendant. From the instructions the jury could take into con-

sideration the fact that there were no tax stamps on the containers in determining whether or not in conjunction with the rest of the evidence the tax had or had not been paid. Most certainly there was other evidence; the admission by the defendant that the seizure was alcohol whiskey, coupled with the fact that Macklin said he used to be a shingle weaver but couldn't do that kind of work any more, coupled with the fact that at the time of his arrest there was found to be \$326 in his possession. (Tr. 25-26).

The Court might well have instructed that it was presumed that the evidence showed from the absence of tax stamps on such a container or containers involved herein that the tax had not been paid and that thereupon the burden of proving that the tax had been paid would be shifted to defendant. The Court did not do this, but put the government on its proof, allowing the jury to consider whether or not a tax had or had not been paid without shifting the burden to the defendant. Indeed, the courts have held in analogous cases under the internal revenue laws where the facts were peculiarly within the knowledge of the defendant that such facts could be presumed. For instance, in *Rossi vs. U. S.*, 289 U.S. 89, where the defendant was charged with having possession and control of a still not registered, the Court held:

“The lower federal courts generally have accepted the doctrine that proof of the custody or control of a still for unlawful distillation of alcoholic spirits is enough to give rise to an inference of lack of registration and failure to give bond *which the defendant must overcome by proof*. *Barton v. United States*, 267 Fed. 174, 175; *McCurry v. United States*, 281 Fed. 532, 533; *Goodfriend v. United States*, 294 Fed. 148, 150; *Giacolone v. United States*, 13 F. (2d) 108, 110; *Seiden v. United States*, 16 F. (2d) 197, 199; *Colasurdo v. United States*, 22 F. (2d) 934, 935; *Cardenti v. United States*, 24 F. (2d) 782, 783; *Mangiaracina v. United States*, 40 F. (2d) 164, *Stark v. United States*, 44 F. (2d) 946, 949, 950. And see *Faraone v. United States*, 259 Fed. 507, 509; *Sharp v. United States*, 280 Fed. 86, 89.”

In connection with proof in such cases it is well to consider Title 26, U.S.C.A., Sec. 327:

“Whenever seizure is made of any distilled spirits found elsewhere than in a distillery or distillery warehouse, or other warehouse for distilled spirits authorized by law, or than in the store or place of business of a rectifier, or of a wholesale liquor dealer, or than in transit from any one of said places; or of any distilled spirits found in any one of the places aforesaid, or in transit therefrom, which have not been received into or sent out therefrom in conformity to law, or in regard to which any of the entries required by law to be made in the books of the owner of such spirits, or of the storekeeper, wholesale dealer, or rectifier, have not been made at the time or in the manner required, or in respect to which the owner or person having possession, control, or charge of said

spirits, has omitted to do any act required to be done, or has done or committed any act prohibited in regard to said spirits, the burden of proof shall be upon the claimant of said spirits to show that no fraud has been committed, and that all the requirements of the law in relation to the payment of the tax have been complied with.”

The conclusion is irresistible that the doctrine of presumption of non-payment of tax as set forth in such cases as *Commercial Credit Corporation vs. U. S.*, 18 Fed. (2d) 927, must of necessity be extended to carry such a rule, or at least the consideration of such evidence, to containers of less than five gallons of distilled spirits.

DEFENDANT CHARGED WITH VIOLATION OF TWO SEPARATE AND DISTINCT STATUTES AND ACQUITTAL ON ONE COUNT WILL NOT BAR CONVICTION ON OTHER AND VERDICT NOT INCONSISTENT.

In *Blockburger vs. U. S.*, 284 U.S. 299, Blockburger was charged with making a sale of morphine not in an original stamped package, in violation of Section I of the Narcotics Act, and making a sale of morphine not in pursuance of a written order of the person to whom the drug is sold, in violation of Section II of the same act. It appears that these two counts were based upon one and the same act. The question involving the appeal was inasmuch as there was but one

sale were both sections violated by the same act and did the accused commit two offenses or only one? The Court said:

“Each of the offenses created requires proof of a different element. The applicable rule is that where the same act or transaction constitutes a violation of two distinct statutory provisions, the test to be applied to determine whether there are two offenses or only one, is whether each provision requires proof of a fact which the other does not. *Gavieres v. United States*, 220 U.S. 338, 342, and authorities cited. In that case this court quoted from and adopted the language of the Supreme Court of Massachusetts in *Morey v. Commonwealth*, 108 Mass. 433: ‘A single act may be an offense against two statutes; and if each statute requires proof of an additional fact which the other does not, an acquittal or conviction under either statute does not exempt the defendant from prosecution and punishment under the other.’”

Following the test laid down in the *Blockburger* case, *supra*, we find that Macklin was charged with the violation of two separate and distinct statutes, one, Section 404, Title 26, U.S.C.A., being a felony, and the other, Section 1181, Title 26, U.S.C.A., being merely a misdemeanor. Section 404 is as follows:

“Removal or concealment of spirits contrary to law. Whenever any person removes, or aids or abets in the removal of any distilled spirits on which the tax has not been paid, to a place other than the bonded warehouse provided by law, or conceals or aids in the concealment of any spirits

so removed, or removes, or aids or abets in the removal of any distilled spirits from any distillery warehouse, or other warehouse for distilled spirits authorized by law, in any manner other than is provided by law, or conceals or aids in the concealment of any spirits so removed, he shall be liable to a penalty of double the tax imposed on such distilled spirits so removed or concealed, and shall be fined not less than \$200 nor more than \$5,000, and imprisoned not less than three months nor more than three years."

and Section 1181 is as follows:

"Removing or concealing articles with intent to defraud United States. Whenever any goods or commodities for or in respect whereof any tax is or shall be imposed, or any materials, utensils, or vessels proper or intended to be made use of for or in the making of such goods or commodities are removed, or are deposited or concealed in any place, with intent to defraud the United States of such tax, or any part thereof, all such goods and commodities, and all such materials, utensils, and vessels, respectively, shall be forfeited; and in every such case all the casks, vessels, cases, or other packages whatsoever, containing or which shall have contained, such goods or commodities, respectively, and every vessel, boat, cart, carriage, or other conveyance whatsoever, and all horses or other animals, and all things used in the removal or for the deposit or concealment thereof, respectively, shall be forfeited. And every person who removes, deposits, or conceals, or is concerned in removing, depositing, or concealing any goods or commodities for or in respect whereof any tax is or shall be imposed, with intent to defraud the

United States of such tax or any part thereof, shall be liable to a fine or penalty of not more than \$500."

The gist of the offense set forth in Title 26, U.S. C.A. Section 1181 is the removal, depositing or concealing, or the being concerned in removing, depositing or concealing any goods or commodities for or in respect whereof any tax shall be imposed *with intent to defraud the United States of such tax or any part thereof*, shall be liable to a fine or penalty of not more than \$500.

The element of removing or concealing or depositing with intent to defraud the United States of the tax is entirely absent from Section 404 which prohibits the removal of any distilled spirits upon which the tax has not been paid to a place other than the bonded warehouse provided by law, or conceals or aids in the concealment of any spirits so removed * * *, shall be fined not less than \$200 nor more than \$5,000, and imprisoned not less than three months nor more than three years.

It takes different proof to establish these two separate crimes although they may possibly be based upon the same act or acts .

Appellant tries to derive comfort from *Morgan vs.*

Devine, 237 U.S. 632, 35 S.Ct. 712. An examination of that authority reveals that it holds in favor of appellee's contention. In that case the defendant was charged in two counts—one with forcible breaking into the postoffice of the United States with intent then and there to commit larceny in such building. The second count charged him on the same date and at the same place with stealing certain property and monies from a United States postoffice. The Court held that these were two separate and distinct offenses. The Court said:

“In *Burton v. United States*, 202 U.S. 344, 50 L.ed. 1057, 26 Sup.Ct.Rep.688, 6 Ann.Cas. 362, the defendant was charged in separate counts with receiving compensation in violation of the act, and also agreeing to receive compensation in violation of the same statute. In that case the contention was that the defendant could not legally be indicted for two separate offenses, one agreeing to receive compensation, and the other receiving such compensation, in violation of the statute, but this court held that the statute was so written, and said:

“There might be an agreement to receive compensation for services to be rendered without any compensation ever being in fact made, and yet that agreement would be covered by the statute as an offense. Or, compensation might be received for the forbidden services without any previous

agreement, and yet the statute would be violated. In this case, the subject-matter of the sixth count, which charged an agreement to receive \$2,500, was more extensive than that charged in the seventh count, which alleged the receipt of \$500. But Congress intended to place its condemnation upon each distinct, separate part of every transaction coming within the mischiefs intended to be reached and remedied. Therefore an agreement to receive compensation was made an offense. So the receiving of compensation in violation of the statute, whether pursuant to a previous agreement or not, was made another and separate offense. There is, in our judgment, no escape from this interpretation consistently with the established rule that the intention of the legislature must govern in the interpretation of a statute. "It is the legislature, not the court which is to define a crime, and ordain its punishment." *United States v. Wiltberger*, 5 Wheat. 76, 95, 5 L.ed.37, 42; *Hackfeld & Co. v. United States*, 197 U.S. 442, 450, 49 L.ed.826, 25 Sup.Ct.Rep. 456.' "

To the same effect see *Carter vs. McClaughry*, 183 U.S. 367, 22 Sup.Ct. 181, *Gavieres vs. U. S.*, 220 U.S. 337.

Rosenthal vs. U. S., 276 Fed. 716, cited by appellant presents a situation different from ours. No more and no less proof was required to support the first and second counts, both charging defendant had in his possession with guilty knowledge property that was stolen. The second count charged the defendant with the same crime at the same time. It involved but one

transaction and required but the same proof. Such a situation is not involved here—one violation dealing with an intent to defraud the United States, and the other removal or concealment of untax-paid distilled spirits. Section 404 refers to distilled spirits alone, and Section 1181 refers to any commodity upon which a tax is or shall be imposed.

Further, in answer to the case of *Hohenadel Brewing Co. vs. U. S.*, 295 Fed. 489, (a third Circuit case) cited by appellant, the cases below go even further than the cases already cited by appellee:

The judges of the Ninth Circuit Court of Appeals, in *Panzich vs. U. S.* (9th C.C.A.), 285 Fed. 871, decided:

“We find no merit in the second assignment, that, inasmuch as Mary Panzich was acquitted of the charge of an unlawful sale, the verdict of guilty of maintaining a common nuisance cannot stand against her. Acquittal of making a sale is not inconsistent with guilt of keeping a place where the purpose is to sell and barter. That no business is done is immaterial, if the place is kept for the purpose of doing business. Under section 21 of title 2 of the National Prohibition Act, any room, house, or place where intoxicating liquor is sold, kept or bartered, in violation of the act, is declared to be a common nuisance, and under section 33 of the same title the possession of liquor by a person not lawfully permitted to possess it shall be *prima facie* evidence that such liquor is

kept for the purpose of being sold, bartered, exchanged, given away, or otherwise disposed of, in violation of the act. It is also provided that the burden of proof is upon the possessor, in any action concerning the same, to prove that such liquor was lawfully acquired, possessed, or used. It seems too clear for argument that, if liquor or wine was found upon the premises, it became incumbent upon the defendants to prove it was lawfully acquired or possessed or used by them.

“We find no reason for disturbing the judgment.”

Seiden vs. U. S. (2nd C.C.A.), 16 Fed. (2d) 197:

“We have held that, when a jury convicts upon one count and acquits upon another the conviction will stand, though there is no rational way to reconcile the two conflicting decisions. *Marshall vs. U. S.* (C.C.A.), 298 Fed. 74; *Steckler vs. U. S.* (C.C.A.) 7 Fed.(2d) 59.”

In the light of the above we submit the verdict should not be disturbed.

Respectfully submitted,

J. CHARLES DENNIS,
United States Attorney;

GERALD SHUCKLIN,
*Assistant United States
Attorney.*

ORIGINAL

7848
No. 7848

IN THE

18

United States
Circuit Court of Appeals
For the Ninth Circuit

UNITED STATES OF AMERICA,

Appellant,

VS.

DEWEY M. SHAFFER,

Appellee.

Transcript of the Record

*Upon Appeal from the District Court of the United
States, for the District of Idaho,
Southern Division.*

OSTER PRINTING CO., BOISE, IDAHO

APR 29 1935

PAUL F. O'BRIEN

CLERK

IN THE
United States
Circuit Court of Appeals
For the Ninth Circuit

UNITED STATES OF AMERICA,

Appellant,

vs.

DEWEY M. SHAFFER,

Appellee.

Transcript of the Record

*Upon Appeal from the District Court of the United
States, for the District of Idaho,
Southern Division.*

NAMES AND ADDRESSES OF ATTORNEYS
OF RECORD

J. A. CARVER,

U. S. District Attorney,

FRANK GRIFFIN,

E. H. CASTERLIN,

Assistant U. S. District Attorneys,

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Attorneys for Appellant.

BENTON F. DELANA,

ELBERT S. DELANA,

Boise, Idaho,

Attorneys for Appellee.

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IN THE DISTRICT COURT OF THE UNITED
STATES FOR THE DISTRICT OF IDAHO,
SOUTHERN DIVISION

DEWEY M. SHAFFER,

Plaintiff,

vs.

UNITED STATES OF AMERICA,

Defendant.

No. 1677

COMPLAINT

Filed Dec. 15, 1931.

COMES NOW, The plaintiff in the above entitled action and complaining of the defendant, alleges as follows, to-wit:

I.

That the plaintiff herein is now a resident and citizen of Boise, Ada County, State of Idaho, in the Southern Division of the District of Idaho.

II.

That on the 15th day of April, 1917, the plaintiff enlisted for military service in the United States Army and served as a member of said United States Army continuously until he was honorably discharged from the United States Army on July 18, 1919.

III.

That while in the said United States Army and during the period between his said enlistment and his honorable discharge, as aforesaid, this complainant, desiring to be insured against the risks of war, applied for a policy of war risk insurance in the sum of Ten Thousand and No/100 Dollars (\$10,000.00), and at the time of said application, authorized the deduction from his service pay of all premiums, that might become due thereon and thereafter there was deducted from his monthly pay certain sums of money as premiums for said insurance.

IV.

That a certificate of war risk insurance was duly issued by the terms whereof the defendant agreed to pay the plaintiff Fifty-seven and 50/100 Dollars (\$57.50) per month in the event that he suffered total and permanent disability, but that no policy of insurance was ever delivered to the plaintiff.

V.

That while the plaintiff was in the military service of the United States, as aforesaid, and during the World War, and while said policy was in full force and effect, and as a result of his military service, the plaintiff herein underwent great hardship and suffering, exposure and fatigue, and on or about July, 1918, became afflicted with tonsilitis, and on or about February, 1919, became afflicted with influenza, pleurisy and pneumonia, and on

or about February, 1919, became afflicted with tuberculosis, pleurisy and asthma, and that plaintiff has continuously suffered from and been afflicted with said last named diseases from a time prior to said discharge and from a time when said insurance was in full force and effect, and this plaintiff is informed and believes, and upon such information and belief alleges the fact to be that as a result thereof, the said plaintiff was, at the time of his said discharge, and at the time when said insurance was in full force and effect, totally and permanently disabled, and that this plaintiff is informed and believes, and upon information and belief, alleges the fact to be that he will always be so disabled and never again able to follow any substantially gainful occupation. That by reason thereof, he became entitled to receive from the defendant, the sum of \$57.50 per month from the date of discharge, to-wit: July 18, 1919.

VI.

That heretofore, and upon October 10, 1930, this plaintiff demanded of the defendant in writing, payment of benefits of said war risk insurance, and on said date filed with the United States Veterans Bureau a written claim for said War Risk Insurance, but that said defendant and said United States Veterans Bureau and the Director thereof, and the Administrator of Veterans Affairs have disputed and denied the claim of this *defendant* and have failed and refused and now fail and refuse to make payment hereunder, and that said claim was

denied by the defendant on December 12, 1931, and that a disagreement exists between the plaintiff and defendant, and has existed since December 12, 1931.

WHEREFORE, This plaintiff demands judgment against the defendant in the sum of \$57.50 per month from the 18th day of July, 1919, together with interest thereon and his costs and disbursements herein incurred, and attorney's fees and that the Court determine what a reasonable fee to be allowed plaintiff's attorneys, and direct the payment of said fees to plaintiff's attorneys.

DELANA & DELANA,
Attorneys for Plaintiff,
Residence: Boise, Idaho

(Duly Verified)

(Title of Court and Cause.)

MINUTES OF THE COURT OF MAR. 5, 1932

The demurrer and motion to strike the complaint herein came on for hearing before the Court by counsel for the respective parties. Whereupon the plaintiff confessed the motion to strike and the demurrer to complaint was withdrawn by the defendant's counsel.

The defendant was granted 60 days in which to answer the complaint.

(Title of Court and Cause.)

ANSWER

Filed June 9, 1932.

COMES NOW the defendant in the above entitled action, and answering plaintiff's Complaint on file herein, admits, denies, and alleges as follows:

I.

Answering Paragraph I of plaintiff's Complaint, this defendant admits the allegations contained therein.

II.

Answering Paragraph II of plaintiff's Complaint, this defendant admits the allegations contained therein.

III.

Answering Paragraph III of plaintiff's Complaint, this defendant denies each and every allegation contained therein; in this connection, however, it is admitted that on November 8, 1917, plaintiff applied for and was granted Ten Thousand Dollars of war risk insurance, and that premiums thereon were paid to include the month of July, 1919. It is further admitted that pursuant to application dated July 2, 1927, and application for conversion of even date, Three Thousand Dollars of plaintiff's war risk term insurance was reinstated and converted to a thirty-pay life policy, effective July 1, 1927, and that premiums thereon were paid to include the month of March, 1932.

IV.

Answering Paragraph IV of plaintiff's Complaint, this defendant denies each and every allegation contained therein; in this connection, however, it is admitted that a certificate of war risk insurance was duly issued by the terms whereof the defendant agreed to pay the plaintiff \$57.50 per month in the event that he suffered total and permanent disability while said contract of insurance was in full force and effect.

V.

Answering Paragraph V of plaintiff's Complaint, this defendant denies each and every allegation contained therein.

VI.

Answering Paragraph VI of plaintiff's Complaint, this defendant denies each and every allegation contained therein, except insofar as said paragraph alleges that a disagreement exists between the defendant and the plaintiff in regard to the payment of said insurance, and in this respect it is admitted that a disagreement exists between plaintiff and the defendant.

WHEREFORE, having fully answered plaintiff's Complaint, defendant prays:

1. That the Complaint be dismissed, and that plaintiff take nothing thereby, and that defendant have judgment for its costs.

2. That if the plaintiff be found entitled to recover on the contract sued upon, that before judgment is entered, he be required to surrender the reinstated and converted policy hereinbefore set forth.

H. E. RAY,

United States Attorney
for the District of Idaho.

RALPH R. BRESHEARS,

Assistant United States Attorney
for the District of Idaho.

Attorneys for the Defendant.

(Duly Verified)

(Title of Court and Cause.)

AMENDMENT TO ANSWER

Filed Feb. 3, 1933.

COMES NOW the defendant in the above entitled cause, leave of Court being first had and obtained, and amends Paragraph VI. of defendant's Answer to read as follows, to-wit,

VI.

Answering Paragraph VI. of plaintiff's Complaint, this defendant denies each and every allegation contained therein.

H. E. RAY,

United States Attorney for the
District of Idaho,

RALPH. R. BRESHEARS,

Assistant U. S. Attorney
for the District of Idaho.

Attorneys for defendant.

Leave of Court to file the foregoing amendment
granted.

CHARLES C. CAVANAUGH,

District Judge.

(Title of Court and Cause.)

MINUTES OF THE COURT OF SEPTEMBER
29, 1934

This cause came on for trial before the Court and a jury, B. F. Delana, Esquire, appearing for the plaintiff, who was also present, and Frank Griffin, Assistant District Attorney and A. L. Freehafer, Esquire, appearing as counsel for the defendant.

The Clerk under direction of the Court, proceeded to draw from the jury box the names of twelve persons, one at a time, written on separate slips of paper to secure a jury. Robert Coffey, Frank Parke, W. E. Platt, S. W. Bilderback, and James J. Attebery, whose names were so drawn, were excused for cause; E. J. Russell, John

Veatch and Walt Whitaker, whose names were also drawn, were excused on the plaintiff's peremptory challenge; and James Bennett and W. J. Vanskike, whose names were likewise drawn, were excused on the defendant's peremptory challenge.

Following are the names of the persons whose names were drawn from the jury box, who were sworn and examined on voir dire, found duly qualified, and who were sworn to well and truly try said cause and a true verdict render, to-wit:

John Fagerstedt, A. B. White, Hugh Crabtree, Harold Packer, Wm. J. Buhler, Hubert Brooks, H. R. McCarter, A. P. Hamer, Chas. Wyman, James E. Stickles, Lawrence Sloan and Dan Regan.

A statement of the plaintiff's case was made to the jury by his counsel after which an oral stipulation of certain facts was entered into by counsel for the respective parties.

Dewey M. Shaffer was sworn and examined as a witness and documentary evidence was introduced on the part of the plaintiff.

After admonishing the jury the court excused them to nine-thirty o'clock A. M., Monday, October 1st, 1934, and continued the trial to that time.

(Title of Court and Cause.)

MINUTES OF THE COURT OF OCTOBER 1, 1934

The trial of this case was resumed before the court and jury. Counsel for the respective parties being present, it was agreed that the members of the jury were all present.

Dewey M. Shaffer was recalled and further examined. Galen Jones, Ray Grimes, Ernest Tegarden, Grover C. Mace, Mrs. Hazel Zamp, John Ellis, A. L. Jamison, Earl Rainey, Edgar Shaffer, J. L. Shaffer, Bill McKenzie, Elbert Harvey, Dale Flora and Allen Wilcox were sworn and examined as witnesses on the part of the plaintiff.

After admonishing the jury, the court excused them to nine-thirty o'clock A. M., October 2nd, 1934, and continued the trial to that time.

(Title of Court and Cause.)

MINUTES OF THE COURT OF OCTOBER 2, 1934

The trial of this case was resumed before the Court and jury. Counsel for the respective parties being present, it was agreed that the members of the jury were all present. On account of illness, it was agreed by counsel for the respective parties that juror Chas. Wyman be excused from sitting further in this trial of the case, and

that the trial continue before the eleven jurors remaining in the box, and that said eleven jurors render a verdict herein. Whereupon, it was ordered that juror Chas. Wyman be excused from further attendance and that the trial continue before the eleven remaining jurors.

Orville Evans, Eb Scrivener, Dr. F. A. Smith, Dr. John Boeck, Dr. Alfred Budge, Dr. O. F. Swindell, Dr. J. L. Stewart, were sworn and examined as witnesses and the depositions of Dr. J. A. Maronde and Dr. M. H. Tallman were read in evidence on the part of the plaintiff.

After admonishing the jury, the Court excused them to nine-thirty o'clock A. M. on Wednesday, October 3rd, 1934, and continued the trial to that time.

(Title of Court and Cause.)

MINUTES OF THE COURT OF OCTOBER 3, 1934

The trial of this case was resumed before the Court and jury. Counsel for the respective parties being present, it was agreed that the members of the jury were all present.

Dr. O. F. Swindell, Dr. James L. Stewart and Dr. Alfred Budge were recalled and further examined as witnesses on the part of the plaintiff and here the plaintiff rests.

Ray Zancher, Roy Franklin, Dan Ackley, C. W. Whiffin and Dewey M. Shaffer were sworn and examined as witnesses and the depositions of Dr. Chas. F. Ensing, Dr. Chas. M. Tinney, Gary Austin, Dr. O. L. Essenson and Dr. D. C. McCulloch were read and other evidence was introduced on the part of the defendant.

After admonishing the jury, the Court excused them to nine-thirty o'clock A. M. on Thursday, October 4th, 1934, and the trial was continued to that time.

(Title of Court and Cause.)

MINUTES OF THE COURT OF OCTOBER
4, 1934

The trial of this case was resumed before the Court and jury. Counsel for the respective parties being present, it was agreed that the members of the jury were all present.

Dr. N. C. Trabau and Dr. P. J. Germon were sworn and examined as witnesses and other evidence was introduced on the part of the defendant and here the defendant rests.

On rebuttal Elbert Harvey, Edgar Shaffer, Bill McKenzie and Dewey M. Shaffer were recalled and further examined, and J. H. Dodd and Howard Grant were sworn and examined as witnesses on the part of the plaintiff and here the plaintiff rests.

On sur-rebuttal C. W. Whiffin was recalled and further examined as a witness on the part of the defendant and here both sides closed.

The Government's counsel moved the Court to direct the jury to return a verdict for the defendant. After hearing counsel on the motion, the Court denied the same. The defendant asked and was granted exceptions to the order.

The cause was argued before the jury by counsel for the respective parties, after which the Court instructed the jury, and placed them in charge of a bailiff duly sworn, and they retired to consider their verdict. While the jury was still out, the Marshal was directed to provide them with dinner at the expense of the United States.

The jury was instructed in case of their agreement to seal the verdict and to return the same into court at nine-thirty o'clock A. M. Friday, October 5th, 1934, and the bailiff was directed to permit the jurors to disband upon their arrival at a verdict.

(Title of Court and Cause)

MINUTES OF THE COURT OF OCTOBER 5, 1934

Counsel for the respective parties being present, the jury returned into court and it was agreed that the

members thereof were all present. The jury thru their foreman presented their written and sealed verdict, which was in the words following to-wit:

(Title of Court and Cause.)

“We, the Jury in the above entitled action, find for the plaintiff, and fix the date of the beginning of his permanent and total disability from July 18, 1919.

JOHN FAGERSTEDT, *Foreman.*”

The verdict was recorded in the presence of the jury and then read to them, and they each confirmed the same.

The defendant was granted sixty days in which to prepare, serve and file proposed bill of exceptions.

(Title of Court and Cause.)

VERDICT

Filed October 5, 1934.

We, the Jury in the above entitled action, find for the plaintiff, and fix the date of the beginning of his permanent and total disability from July 18, 1919.

JOHN FAGERSTEDT, *Foreman.*

(Title of Court and Cause.)

JUDGMENT

Filed October 6, 1934.

This Cause, Coming on regularly to be heard on September 29, 1934, before the Court and Jury, Benton F. Delana of the firm of Delana & Delana, appearing as counsel for the plaintiff, and Frank Griffin, Assistant United States District Attorney, and A. L. Freehafer, attorney for the United States Department of Justice Bureau of War Risk Litigation, appearing as counsel for the defendant. A Jury was duly drawn, empanelled and sworn, and the plaintiff and defendant introduced evidence.

Whereupon, the Court submitted the cause to the Jury on October 4, 1934,

Whereupon, the Jury retired and on October 5, 1934, returned to Court, counsel for both parties being present, and presented their written verdict in words and figures as follows:

“IN THE DISTRICT COURT OF THE UNITED STATES, IN AND FOR THE DISTRICT OF IDAHO, SOUTHERN DIVISION.

No. 1677

VERDICT.

DEWEY M. SHAFFER,

Plaintiff,

vs.

UNITED STATES OF AMERICA,

Defendant.

“We, the Jury in the above entitled action find for the plaintiff, and fix the date of the beginning of his permanent and total disability from July 18, 1919.

JOHN FAGERSTEDT, *Foreman.*”

The said verdict was duly recorded in the presence of the Jury, read to them, and they each affirmed the same.

WHEREUPON, Upon such verdict, It is Ordered, Adjudged and Decreed, And the Court does hereby order, adjudge and decree:

I.

That the plaintiff, Dewey M. Shaffer, became and was totally and permanently disabled on the 18th day of July, 1919, and ever since said date, has been and now is totally and permanently disabled, and that there is due and owing from the defendant to said plaintiff, Dewey M. Shaffer, on the policy of war risk insurance as described in the complaint in this action, and that

the plaintiff do have and recover from the defendant the sum equal to the accrued payments now due for Fifty-seven and 50/100 Dollars (\$57.50) per month from the 18th day of July, 1919, to and including the month of September, 1934, or a total sum of Ten Thousand Five Hundred Twenty-two and 50/100 Dollars (\$10,522.50).

II.

IT IS FURTHER ORDERED, ADJUDGED AND DECREED, That ten per cent of all sums to be paid pursuant to this judgment is hereby fixed as a reasonable attorney's fee to be allowed to Benton F. Delana, as attorney for the said plaintiff, the same to be paid to the said Benton F. Delana by the Veterans Administration of the United States, or the Agency having charge of the payment of the same, out of any and all payments to be made to the said Dewey M. Shaffer, or to his estate, or to the beneficiary or beneficiaries under said insurance policy.

Dated this 6th day of October, 1934.

CHARLES C. CAVANAH,
District Judge.

(Title of Court and Cause.)

BILL OF EXCEPTIONS

Filed April 10, 1935.

Be it remembered that the above entitled cause came

on for hearing before the Honorable Charles C. Cavanaugh, Judge of the above entitled court, sitting with a jury at Boise, Idaho on September 29, 1934, and the trial of said cause continuously thereafter until the return of the verdict of the jury on October 5, 1934 and until the entry of the judgment herein on October 6, 1934, the issues being formed by plaintiff's complaint and the defendant's amended answer thereto, Benton F. Delana of Delana and Delana, Boise, Idaho, appearing as attorney for the plaintiff and J. A. Carver, United States Attorney for the District of Idaho by Frank Griffin, Assistant United States Attorney and A. L. Freehafer, Attorney for the Department of Justice, of Boise, Idaho, appearing as attorneys for the defendant, whereupon and whereafter the following proceedings were had in respect of the assignment of errors involved in this appeal.

Plaintiff made his opening statement.

(DR. O. F. SWINDELL was called as a witness for the plaintiff and testified as follows:)

DIRECT EXAMINATION

Q. Now, then, will each one of you doctors listen to this question I am about to ask here. Each one of you doctors may assume the following facts: That Dewey Shaffer enlisted in Company B, Second Idaho, on April 15th, 1917; that he went overseas on December 24th, 1917; that he debarked at Liverpool, England, and went to LeHavre, France; in January, 1918 he landed at Camp

Dijon, France; that along in March, 1918, he took quite a severe cold and had a cough; that he had a running of the ear, that he was confined to quarters for a period of from two to three weeks; that after being confined to quarters for two or three weeks he was placed on light duty consisting of taking dishes and victuals to the 'mumps' camp, where some boys were confined with the mumps; that he was placed on regular duty drilling heavy artillery until July 14th, about that time; that during this time Mr. Shaffer coughed continuously, that he had some difficulty in breathing; that on July 14th he contracted a heavier cold than the one had before, and was placed in a hospital and spent four days there; that during that time he had night sweats and his cough was more severe; that he was returned, not to duty, but to light duty, the light duty consisting of helping the cook in the kitchen and waiting on table, and washing dishes; that after he returned to light duty, he noticed himself and his fellow companions noticed that he had a cough and that his cough increased, and that his breathing was difficult, and that a part of the time he was not able to be on light duty; that through July and August the weather was pleasant and they were at the Chateau-Thierry on the front, and that he went to the Meuse-Argonne, the St. Mihiel front, and from August the weather was very sloppy and wet underfoot, and they wore rubber boots and big hob-nailed shoes, that they camped out in the open and laid on the ground, that it became foggy and

the weather became colder and disagreeable; that he had night sweats throughout this time, and that one of his buddies said that he had night sweats and his breathing was difficult, and several of the other boys with him said the same thing; that they would come in at night and go to the kitchen where he was supposed to be waiting, and that some of the time he would be in bed and not get up, that he was coughing and wheezing, and that his buddies would go in and see if there was anything they could do for him; that his cough increased, and the difficulty in breathing increased, and that at Armistice time he was placed in his billet, and that his cough increased up until about December 2nd, and his hard breathing increased. On December 2nd they started for France and traveled in trucks,—

THE COURT: What do you mean when you say 'they started for France?'

MR. DELANA: I beg your pardon. I should say they started from France and into Germany, and that all except two or three nights they stayed in the open and that it was snowing and raining and sleeting, and that Mr. Shaffer's cough became worse and his breathing more difficult; that about December 22nd, about three days before Christmas, he was taken off light duty and had missed a number of days; that he was finally taken off entirely and was confined to his quarters; that on December 22nd, 1918, this happened, and that he remained on light duty, and while he so remained his

cough increased and his hard breathing increased; that on February 14th, 1918 when he was placed in the hospital, and he remained in this hospital from February 14th until some time in April, and that at the time of entry to the hospital he had a temperature of 101 in the morning, and an afternoon temperature of about 103; that the admission to the hospital occurred on February 14th, 1919 as shown by the admission card; that under date of February 14th, 1919, the diagnosis is: Pleurisy, serofibrinous. On February 15th the service records show, lower lung, lower and middle lobe of right lung show numerous rales and increase in vocal fremitus; under February 20th the record shows the diagnosis of increased vocal fremitus and subcrepitant rales in right lower; February 24th shows by a lung examination flatness over right base, posterior, and the breath sounds about the same area, temperature 102; on February 25th the chest was tapped in the sixth interspace and mid-auxiliary line and 100 c.c. of clear yellow fluid withdrawn; and later on March 8th it shows a few moist rales in the right lower lung. Sheet 2 of this clinical record shows pleurisy, serofibrinous, with tachycardia; on March 20th, roughened breath sounds over the entire left chest, and no rales, left chest shows marked increase in vocal fremitus over right upper, absent breath sounds and diminished fremitus right lower; on March 23rd, pleurisy continues hard; March 26th the same, vocal fremitus still exaggerated in right upper, with exaggerated

breath sounds on left, diminished fremitus over right lower, pulse continues high; April 3rd, developed,—I can't read that word, but the next is angina; April 15th, patient very anemic. You may assume that when he got to New York,—by the way, he was taken to France and landed in Brest and was kept in a hospital for a week or ten days, and then he was brought in a hospital ship to New York, and placed in a hospital and diagnosed in New York on May 30th as pleurisy, with effusion; he was brought from New York to Salt Lake City in a hospital train with nurses, and while in the service it is testified that along in March one of his buddies went to visit him and he was very thin and very emaciated, and very poor, he was so listless that he didn't carry on any conversation, and one of his buddies went to visit him while he was in the kitchen and he passed him about five feet, and didn't know him, and one of his buddies who knew him as a boy testified that he was in such a condition that he didn't recognize him within about five feet of him; another buddy went to visit him and he walked with him, and when he was walking three blocks sat down twice to rest, and he walked as if he was very weak, and he didn't recognize him until he walked up within a half block of him; that he then took him and placed him on a billet and gave him a can to spit in, that he was weak and emaciated; that he was visited by his folks while he was in Salt Lake City on about July 4th, 1919, and while there at Fort Douglas in Salt Lake City he kept

asking his doctor to get out of the service, telling him that he wanted to be discharged, and his folks left him there, and he kept on asking for his discharge from service, and the doctor told him that he was not ready to release him, but finally on July 18th, 1919, he was discharged from service, and the manner of discharge was that he was sent down with fifteen or twenty other fellows, and they went to a room and he was presented with some blanks, some papers, for his signature, and he signed them; that they were not read to him; that he was not examined by a doctor at the time of discharge; and further that about the date of his discharge he was presented with a typewritten or printed blank whereon this question appears: 'Have you any reason to believe that at the present time you are suffering from the effect of any wound, injury or disase, or that you have any disability or impairment of health, whether or not incurred in the military service?' and the typewritten answer appears: "No." And on the same date his superior officer made a certificate which reads, "I certify that the soldier named above has this day been given a careful physical examination, and that it is found he is physically and mentally sound." You may assume further that immediately following his discharge from the service he returned home; that he got off the train or car and walked about a mile home, and his sister went to meet him and didn't recognize him because of his paleness, weakness, and change in his condition; that that night he slept

with his brother, and that he kept his brother awake by coughing and wheezing, and the next night his bed was changed and he was placed on the front porch, and thereafter his sister and his father and brother slept in rooms that were away,—they were the second rooms from him, and they heard him coughing and wheezing; that about the same night of the day after he got home he went to a doctor at Middleton, Doctor Hammer,—Doctor Hammer is not able to testify at this hearing,—and within two weeks after his discharge he went to Doctor Gue, and he told him to go to the mountains; that Doctor Gue had taken some X-rays, and that he, Mr. Shaffer, had made an attempt to get the X-rays but was not able to. That he went to the mountains and his chest pained him more, and his cough was worse, and that he came back within a couple of days; that he came back to Boise and went to Doctor Tolman; that he went there and was given a physical examination, a sputum examination and an X-ray was taken; that Doctor Tolman also punctured his lung and took from him a cup to a cup and a half of yellow fluid; that Doctor Tolman testified that he had diminished breath sounds, positive sputum, limited motion of the chest, and that the X-ray and the entire examination had shown that he was moderately advanced with a tubercular condition, active condition, that Doctor Tolman treated him for about six weeks, and that he stayed at home the rest of the fall and winter, and went to bed in the mornings, and gen-

erally again in the afternoons; that he just laid around and didn't do anything; that his cough continued and his hard breathing continued, and that he bothered his folks and kept them awake some of the night, and along in the spring of 1920 that he leased a part of his father's place,—you may assume, first, that during the fall that he didn't play around with his boy friends; some of his boy friends told about their going swimming, and his having trouble walking about half a mile, and he didn't go in swimming with the other boys. During the fall in playing games there since he had come home, he didn't play in any of the games but just watched them, and didn't participate. He leased his father's place, or a portion of it, but his father put in most of the crops; that Mr. Shaffer stayed in bed most of the time and his cough continued, and his hard breathing also continued, and his father and the rest of the family helped him during that year; that about June, 1920, his brother-in-law came over and stayed with him, and did most of the work on the place, Dewey went out to help run a binder but all that he did in assisting in the cutting of the grain was to bring the horses, and to relieve his brother-in-law at mealtimes; and that he did some shocking of grain in the evenings for a couple of hours, and that while he was doing this shocking he had a coughing spell, and that his brother helped him to the house; he didn't help with the threshing except that he was kind of the supervisor, but did not do any of the work, and stayed in

the house most of the time; that during September his brother-in-law had a job loading gravel, and Mr. Shaffer attended to the trap on the gravel pit; the gravel was loaded from a trap door and Dewey's job was to scrape the loose gravel into the truck, and also to keep track of the number of loads that were taken out; he was able to do this work for about half of the time that he was there; while he was there working he had a bunk on which he could rest, and he rested probably about half of the time; that one time his father came to visit with him and he was weak and emaciated and looked tired, and his father volunteered to relieve him, and did relieve him that day; that in the winter of 1920 and '21 he stayed at home and didn't do anything; that is, he didn't do anything a great deal of the time but just stay around the house lying down on the cot or on the bed; that in the spring of 1921 he was married and rented a ranch near Kuna; that he went out and endeavored to plow and was seized with a pain in the chest and with coughing and this hard breathing which continued; he went to the house and he was relieved there at this job of plowing by his brother and some hired help, and he did none of the harrowing of the ground, but when it was ready for the grain he went out and tried to drill, and while drilling he was seized with a coughing and wheezing spell, and his wife went out and relieved him and did the rest of the drilling, and that he endeavored to run a mowing machine during the time they were putting up hay, and was

seized with a coughing spell and didn't mow any more of the hay; that during the haying he endeavored to pitch hay on the loads and became exhausted, and then he went to the haystack and tried to handle the fork there, and that he did that until shortly after noon when he was seized with a coughing and wheezing spell, and he went to bed for the rest of the afternoon; that at the time the grain was harvested it was done with a combine harvester and the people that did this harvesting with this combine, to pay for it and the help, took all of the grain except nine sacks; that the crop was put in by his brother-in-law, and other relatives as I have stated; on July 24th, 1921, he went to his brother-in-law's place, where they were going to get together and go to a Fourth of July celebration, that he got there in the evening and was feeling fairly well, that in the morning he was seized with a coughing and wheezing spell, and they took him on a cot to the celebration and that he laid on the cot most of the day at the celebration; that in the fall of 1921 he went with his wife to pick prunes; that he went out about seven o'clock in the morning when the rest of them went out, and that he was seized with a coughing spell, and that after that day he didn't go out until after the dew was off; that while he was working at this prune picking the climbing of the ladder and the reaching up for the prunes would bring on these coughing and wheezing spells and he would have to go to the tent and sit down and rest; that during the day this

would occur several times; that he went to Doctor Gue again for treatment; that during the latter part of September he went down to Fruitland and got a job trucking, but that he couldn't do this, and then they gave him a job as janitor, picking up the loose boxes, broken boxes and pieces and sweeping out, and that the sweeping would cause a lot of dust and it would bring on these coughing and wheezing spells, and his wife would do the sweeping for him. About the middle of October he went to Payette and got a job in a restaurant washing dishes, but that the heat and the steam there caused this coughing and wheezing, and that during the winter of 1921 and 1922 he and his wife ran a cream station in Payette, and that consisted of taking cream in big cans, but they would have to wash the cream cans and the powder they used in cleaning the cans caused him to cough and wheeze. His wife did the washing of the utensils. That they had to test the cream, and in making this test they used acid, and that this acid caused him to cough and wheeze, and his wife would do the testing of the cream, and also his wife opened up the cream station in the morning, and that he didn't come until all the way from nine o'clock until noon, that he was in bed a good deal of the time, and was sick a good portion of the time; that they kept this station until July, 1922, and that he then went to Glenns Ferry and got a job as hostler's helper, and that job was getting up and down on the engines and loading coal and water,

and throwing switches for the engineer, and in doing that it would bring on these hard coughing spells and he lost about ten days of the time he was there, and that during that time he lost considerable weight; that he did nothing further until September, and at that time he applied for vocational training, and at about the same time he was examined by Doctor Budge; he was given a complete physical examination, his chest was percussed, and examination was made by stethoscope, examination of the sputum, and the examination of the sputum showed that it contained tubercle bacilli, and the diagnosis was that he was suffering from active tuberculosis and bronchial asthma; that he then started to school in September, and that he missed some days and half days; that he came home early in the afternoon and that he was attended by Doctor Budge, and that at that time he was taking for this asthma hypodermics; that before Christmas of 1922 he had a severe attack of choking and wheezing, and that Doctor Ensign of the Veterans Bureau, and later Doctor Budge was called and gave him a hypodermic, which gave him some relief; that he continued in school until 1923, that he was sent to the University at Seattle, Washington, with the Government, and that his condition there was worse, his cough was severe, and he missed more school, and his sister testified that when he came home he was so weak that he couldn't walk upstairs, and he had night sweats, and that his pajamas and bedding were wet; and his service

record shows that he had night sweats while he was in the service, and his buddies have testified that he also had night sweats while he was in the service, and his sister testified that immediately after he got home he had night sweats, and that it was necessary to change the bed because the bedding would be wet. That he stayed in school and missed some time, until March, 1923, when he was taken to a private hospital in Seattle; that he was confined in that hospital about ten days, and then he was taken to Portland to the Veterans Hospital and remained there until about July 10th of that year; that he was by the doctors at that time sent out camping; that he went back to Seattle and got his camp equipment and on the way he was seized with a wheezing and coughing spell, and on arriving at Seattle he was weak, and all that night he was unable to sleep until toward morning and then he was allowed to sleep until noon the next day; that he left Seattle and went out on this camping trip at or near the Dalles, Oregon, and he was to be gone for a period of about three weeks, but that he went back to Portland in a couple of days; that he was released from the Portland Hospital with the advice to go to a drier climate, and that they went to Long Beach, California, taking fifteen days to make the trip, because they were driving slow on account of his condition, and he was not able to go very far at a time, he was weak and emaciated; that they got to California and rented an apartment and the next day he was asked to move

on account of the disturbance of the other guests by his coughing and wheezing; that along in September, 1923, he was visited by one of his ex-servicemen who testified that he had a very severe coughing spell, and that he burned some kind of stuff and inhaled it, and it seemed to relieve him; that he got a job with a newspaper and had a crew of men or boys under him, and that he would take the crew out and while they were working he would rest, if he wanted to, and that he continued to oversee this crew for about five weeks; that he then got a job with a real estate firm and made two sales and earned \$45.00 in about five weeks; that in December, 1923, he applied for vocational training and was given vocational training, continuing with bookkeeping; that he continued until September, 1924, and that he and his brother and his wife testified that he was out of school days and parts of days at a time, that he would come early in the afternoon, and that he had a great deal of difficulty at night in breathing, and with his coughing, that he would get up and walk around sometimes, and that sometimes at night he would get up and he and his wife would ride out in the hills as the air seemed to give him relief; that the doctor would give him hypodermics, and that in December, 1923, to September, 1924, he went,—that in December, about Christmas time, it was Doctor Moronie who gave him the hypodermic to relieve him, and that between December, 1923, and September, 1924, he would take hypos as high as twenty-five or thirty

times; that in September, 1924, the Government changed him from bookkeeping in this vocational training to electrical fixtures, to a repair man's work, and that he was with one firm for about three weeks and that during that time he missed a good deal of time; that he went to Doctor Moronie, that he was coughing and wheezing more, and that while he was doing this work he went out riding more often at night; that he worked for the Hale Electric Company for forty-seven days, and that after he had been working there for about six days he was seized with a violent coughing and wheezing spell and went home, and was there for about ten days; that he went back to work again and had another spell and was carried out by one of his fellow workers; that he then went from the Hale Electric Company to the Wilkerson Shop Company and took the same kind of training; that his wife testified on arriving home at night he would go to Doctor Moronie as high as sixty times in that year, and Doctor Moronie testified that he examined his chest, percussed, examined it with a stethoscope and took a sputum test, and testified that the sputum was positive tubercular, that he had a temperature, and that his pulse was high, that he had a wheeze, and that he had to relieve him by giving him a hypodermic; that he treated him during the two years while he was taking vocational training, and on an average of every ten days and sometimes oftener, and sometimes less, and in the fall he was taking training and that he got worse; he and his wife

then got a house at Alcadena and he quit vocational training and later came back to Eagle, Idaho, and that he was examined in 1925 by Doctor Smith and Doctor West, and that Doctor Smith testified that he was suffering at that time from tuberculosis and asthma, that he had a temperature and that his pulse was high, and that there was a limitation of the chest movement; that at about the same time he went to Doctor Budge and upon an examination of him by Doctor Budge who testified that he was suffering from active tuberculosis and that both lungs showed diminished breath sounds; that he stayed out home with his parents that winter and did nothing, and that in the spring of 1926 he rented the Ryles place east of Middleton, that in the spring he went out to plow and was seized with a coughing spell, and at one time his sister relieved him, and at another time his brother relieved him, and that in the drilling of the grain he did the drilling by working for two or three hours a day, that in the irrigating time he didn't do much of that, but that at one time he was irrigating and he was seized with a coughing spell and one of his neighbor's boys came along and put him in his car and took him home; that in the haying time he went out with his father to pitch hay and he was seized with a coughing spell, and he got one of his neighbors to take him to his place and he rested the rest of the day, and in pitching he would pitch on the bottom of the wagon until it got up high, and then the other two of them put on the rest,

and he would sit around in the shade and rest; in threshing time he did nothing except manage the crew, and during the cutting of the grain his brother ran the binder and he didn't do any shocking, but at threshing time he did nothing, except as I say, to manage the crew, that is, by the way of working. His neighbor had a thresher and he got a job hauling grain for a man by the name of Spillman, and his job was to haul the grain from the thresher to Middleton and unload it; he endeavored to handle it but it brought on coughing spells and he was unable to do that; that he has some clover to cut in a field and he went out at four o'clock in the morning and cut until the dew was off, and he got along fairly well the first morning, and that other days he didn't get along; that in shocking the clover he went out the first morning,—or, rather, the second morning, after he was out about half an hour he was seized with this coughing and wheezing spell and the rest of the time he did nothing, he didn't go back at this and did not do anything the balance of the fall; that in September he took a series of eight treatments from Doctor Elbert of Caldwell, and that same summer he went out with his brother to run a dyking machine, and this was dusty and he was unable to do this, and he hired one of the neighbors to come in and relieve him, and he went to the house; in 1927, as to his farming operations he testified he had to hire a lot of help and his expense was high, that the income was about \$125.00 in his favor,—that was not including the

depreciation of his car and the running expense and the living expense of himself and wife; in January, 1927, he ran the same place,—that is, in 1927, I should say, he ran the same place again, the Ryles place, for the second year, and he went out to plow and fence and tried to harrow, and was unable to do so; he was seized with coughing spells and went to the house; he didn't do any plowing or any harrowing; in harvest time he went out to relieve the regular man during the meal time; he didn't shock any grain at all, and during the threshing time he didn't do anything except just boss the job, and during the threshing he was seized with a very severe coughing and wheezing spell, and his brother and a neighbor boy helped him to the house, and he was not able to walk at that time without their help; he was forced to stop two or three times on the way, as these people testified that he had a hemorrhage, and that he raised about a cup or a cup and a half of blood on the way to the house; that he had a coughing spell that night, and they were afraid they were going to lose him; Doctor Budge was called about five o'clock in the morning, and he came and administered a hypo; the next night he had a severe spell again and became unconscious; that his father and brother took him riding at night and in the early morning to get relief from these severe spells of coughing and wheezing, that he was taken to Doctor Pittenger at Boise and thereafter for about a week they would go out riding at night to get relief from these severe spells; in

July 1927 he applied for reinstatement of \$3000 of the \$10,000 insurance policy; on the first page the question is asked: "Are you disabled on account of any injury or disease?" and the typewritten answer was, "Yes." And in asking on the following page whether or not he was totally and permanently disabled, the answer was written in, "No," and the explanation is that at the time he came out of the service up to 1927 he did not know that war risk insurance covered disability, and that he didn't know it until 1929 when he went to the hospital here, to the Veterans Hospital, and was told by Doctor Stallings; he testified the only disability he knew anything about was compensation disability; that he gave his history as having had treatment by Doctor Tolman for his lungs, by Doctor Gue for his lungs, Doctor Smith for his lungs, Doctor Morondie for his lungs, and these were in 1920, 1926, 1924 and 1925, and in answer to the doctor's questions he answered that he was treated in 1919 and 1920 for lungs, and also in hospital No. 77 in Portland, Oregon; that in August, 1927, he went to Doctor Boeck in Boise, and Doctor Boeck gave him a series of twenty-four treatments, and he had these treatments and that at the time he gave him these twenty-four treatments that he didn't get better and he advised him to change climate; Doctor Boeck said he was wheezing so badly that you could hear him for quite a distance; that he went to Yakima, he and his wife, got a job there in an apple warehouse, and he was there for about four weeks,

and he worked twelve days out of the four weeks; he went to Doctor Middleton at Yakima, and he was given a course of treatment for asthma, taking adrenalin as high as twelve times at night; he left Washington and went to Portersville and then he went to Lindsay. This job he had in the warehouse at Yakima trucking apples, or fruit, brought on a severe coughing and wheezing spell, and he was then given a job scattering papers around for the boxes, the fruit boxes, and this is a job that a school boy did before him; that he was taking as high as fifteen hypodermics of adrenalin during a night; he went to California and he rested there during the winter and about February 1st he leased a service station and sold oil and gas and accessories, and he got along fairly well for about two weeks, but he had the same inability to sleep, and his wife opened up the station in the morning and he would come all the way from nine o'clock until twelve, and they had a mechanic there to help with the work; his wife testified that there was about a third of the time that he was seized with these coughing spells, and sometimes was carried out, and that at one time he was taken to the Community Hospital, and there he was given some treatment by being given hypos; that he stayed there about half a day and then his wife and some friends took him home, and he had to be helped into the house; that along in April, 1928, he took about thirty hypos from Doctor Arlett, and that his condition was about the same, and he came back to

Eagle, and he was treated by Doctor Budge for asthma, and that about September 1st, 1928, he went to Washington, to Cashmere, Washington, and got a job as foreman in an orchard, and his duties there were to look after the pickers, and his testimony is that he worked perhaps a half, or a little more than half of the time while he was there, and the rest of the time he was in the tent resting, and upon going to the tent at noon or in the evening his wife or brother would find him lying down, he was taking adrenalin for relief practically every night; that he went back to California about October 1st, and got the same job that he had before, that is, distributing papers to the packers of this fruit to line the boxes with, that this took him three or four hours a day, and that he came back to Eagle after that about Christmas time in 1928, and stayed until March of 1929; that his condition got worse and he had more night sweats, more trouble at nights, and in March, 1929, he was treated by Doctor Budge for his trouble, and at that time he had a temperature; in March, 1929, he left and went to Arizona. The testimony is the first day they traveled about a hundred miles, and they took about fifteen days or two weeks to make the trip, traveling very slowly because of his weakened condition. They stayed there for about five weeks, and he got worse, and then he went from there to Ely, Nevada, and got a job for about two weeks as clerk in a hotel, and that he was taking adrenalin all of the time and taking it on the job as clerk at

the hotel, that he was having trouble and was taking this adrenalin when the boss caught him taking it one evening and he was discharged; that they got a room in an apartment house there and the landlady complained of his disturbing the other people, and they were required to move out; that they came in July, 1929, back and he went into the Veterans Hospital June 30th,—or rather on June 15th, 1930, and was doctored at that time in the Veterans Hospital and was confined to bed in the ward there taking tubercular treatment, rest in the morning and afternoon, and on getting out of the hospital he went to the mountains for his health. After he had been there for a short time he endeavored to help a sheepherder to butcher a sheep and it brought on a severe coughing spell and wheezing spell, and he was in bed for three or four days. Then he made a trip to Loon Lake, which was about five miles, and it took him six hours to make the trip, and he was there a short time when he got a sore throat and had pains in his chest, when he came back to Boise, and the doctor then sent him to the hospital, that is, Doctor Budge after giving a complete examination and taking a test of his sputum, and the sputum was positive, testified he had an active tubercular condition, complicated by pleurisy and asthma. Mr. Shaffer stayed here in Boise until November, 1930, when he left and went to California. He thought that it would be better in California for his health. They took an apartment in Venice but he disturbed the people

so much that he was requested to move, and they did move. They moved back to the east side of Los Angeles and lived there until they returned to Boise in February of 1931. During all of this time he was taking adrenalin, all winter. They lived in Boise until August, 1931, and he didn't do any work. A Mr. Wilcox testified that he slept with him in February, 1931, and that he was getting up in the night and taking adrenalin; that his bed was wet with night sweats, and that in August, 1931, he went to visit his folks at threshing time in Eagle, that he wasn't doing any work but being around there the dust of the thresher brought on a coughing spell, and about April 1st, 1932, he went up to Jordan Valley to cook; he was supposed to bring in the wood and the water, and his wife went up there to take this job; he was supposed to bring in the wood and water, but in chopping the wood and carrying the water it brought on choking and coughing spells, and made him very weak, and in carrying the water it had to be carried up an incline for about four hundred yards, and that brought on severe coughing spells, and thereafter the other men there carried the water for him; that in washing dishes the steam and the heat would bring on wheezing and coughing spells; that the last severe coughing spell he had, one of the boys went to get a car to take Mr. Shaffer to Jordan, and that during the time he was gone for the car Mr. Shaffer was taking adrenalin, and that when he came back they took him to Jordan Valley, and they

had to stop for him to take his adrenalin, and that when he came back they took him to Jordan Valley, and they had to stop for him to take his adrenalin because of the severe coughing spells; that in March 1932 an X-ray was taken at St. Luke's, and according to the testimony of Dr. Stewart it showed tuberculosis in both lungs; that about May 1st, 1932 Mr. Shaffer moved to Caldwell, Idaho, and that moving from one place to another there they had only personal effects to move, and he would have to make three or four trips in order to move them; that he had to move from one place to another because he was up in the night, coughing, and he disturbed the other people and they were requested to move, and that Mr. Wilcox testified that he and his brother and Mr. Shaffer were going on the Fourth of July on a camping trip up on Shaffer Creek, that they were to stay three or four days, that he was up all night the first night,—about all night,—coughing and wheezing, and he went to bed about sun-up in the morning and slept until noon, and that that afternoon they loaded up the car and came back home; that the last of July he went to visit his sister in Seattle, intending to stay about three weeks, that upon getting there he was seized at night with a coughing and wheezing spell, and they were up most of the night and he was taking adrenalin and didn't go to bed until the next morning; that he stayed the next night, and the third morning they left to return home; that he was in bed then about a week or ten days,—or, rather, about

ten days or two weeks. Mr. Wilcox testified he was around there for about three weeks, and that he often saw him taking adrenalin, and that he often woke him up; that about January, 1933, the only work he did,— he did no work in 1931, and in 1932 the only work he did was in a sheep camp for about a week; in 1933 all he did was to help install some streets at Caldwell for the disabled veterans, and in 1933 he had another severe spell. His temperature was taken at 100 degrees and eight-tenths; that in the latter part of September, or in the month of November he moved to another place in Caldwell, carrying his personal belongings, and that brought on a coughing and wheezing spell, and a man helped them to move. He did no more work in 1933, and in January, 1934, he was seized with a severe coughing spell, and his friend Elbert Hardy testifying that he was coughing severely, and that he went to the bathroom and that he could hear him coughing and wheezing from there; that he moved to Boise in March, 1934, and in March, 1934, he got a job with the FERA. His brother would take the horses to the job for him and take them home in the evening, and he would go home in a car; his job was driving a team, but on this job his coughing and wheezing increased and he worked for two days the first week, and one the next, and two the third. From 1928 up to the present time Doctor Budge has testified that he has been attended by him once or twice a month, that he was suffering with active tuber-

culosis and pleurisy at the times he was examined; and Doctor Swindell testified that he had active tuberculosis in both lungs, and a sputum examination revealed positive sputum on June 27th, and on July 6th and on July 27th, he had tubercle bacilli. Assuming the above facts, and assuming the definition of total and permanent disability to be, that is, total disability is any impairment of mind or body which renders it impossible for the disabled person to follow continuously any substantially gainful occupation; and total disability shall be deemed to be permanent whenever it is founded upon conditions which render it reasonably certain that it will continue throughout the life of the person suffering from it, now, Doctor, I will ask you, assuming these facts, and taking this definition, whether you have an opinion as to the total and permanent disability of the plaintiff at the time of his discharge from the army on July 18th, 1919?

A. Yes, sir.

Q. I will ask you to state whether or not, in your opinion, he was totally and permanently disabled at the time of discharge from the army on July 18th, 1919.

MR. GRIFFIN: I would like to ask a question.

(Questions by Mr. Griffin:)

Doctor, in this hypothetical question it was called to your attention that when the plaintiff separated from the service of the United States that this question was asked: "Have you any reason to believe that at the present time

you are suffering from the effects of any injury or disease, or that you have any disability or impairment of health, whether or not incurred in the military service?" and the answer to that is "No." And the plaintiff explains that by saying he wasn't asked that question; that there is a certificate here reading, on plaintiff's exhibit 8, by the commanding officer, "I certify that the soldier named above has this day been given a careful physical examination, and it is found that he had pleurisy R on February 14th, 1919," and that is signed by William F. Burns,—Burr, I guess it is, Major, M.C.U.S. Army. Plaintiff testified that he did not receive any examination. Now, Doctor, which of these do you believe? Do you believe the testimony in the hypothetical question, or do you assume the record as contained in Plaintiff's Exhibit 8 as being true?

THE COURT: He is asking you which of these do you take into consideration when you give this opinion?

MR. DELANA: He might take both of them together.

A. You want me to state which one I think are the facts?

Q. (By Mr. Griffin): Yes.

A. I think both are the facts. I think the plaintiff's memory is probably at fault, when he said he didn't receive a physical examination.

Q. (By Mr. Griffin): Do you think that both are true?

A. I think that both men were telling the truth.

Q. (By Mr. Griffin) And in your opinion which are you going to give the greater weight to, the evidence contained in plaintiff's exhibit 8, that I have read, or the testimony of the plaintiff that has been read to you in the hypothetical question, in arriving at your opinion?

A. Regarding this examination?

Q. (By Mr. Griffin) Yes, regarding that.

A. I think I could disregard both.

Q. (By Mr. Griffin) You are going to disregard these?

A. You mean the fact that he didn't have a physical examination when he was discharged? I would probably give greater weight to your record there of the examination.

Q. (By Mr. Griffin) To this record in plaintiff's exhibit 8?

A. I think I am a little confused about the two facts.

Q. (By Mr. Griffin) It will be necessary in giving your opinion to consider the record as true, or the testimony as true,—you have to say that one or the other,—both cannot be true.

A. I will give the greater weight to the testimony of the plaintiff.

Q. (By Mr. Griffin) So you have to disregard plaintiff's Exhibit No. 8?

A. What is Exhibit No. 8?

Q. (By Mr. Griffin) That is what I read to you where it contains that he says there was nothing wrong with him, and also the certificate of the examining officer, that is plaintiff's exhibit 8.

A. I will accept the testimony of the plaintiff.

Q. (By Mr. Griffin) And disregard the other?

A. Yes.

Q. (By Mr. Griffin) Now, Doctor Swindell, when the plaintiff made application for reinstatement of a yearly renewal insurance under date of July 2nd, 1927, in answer to question as to his condition, "Are you in good health?" he answered that he was in fair health. What consideration will you give that in your opinion?

A. I will regard that, but I have a feeling that the man didn't realize his physical condition when he made the statement.

Q. (By Mr. Griffin) You believe that this exhibit, Defendant's Exhibit No. 9, is wrong, and the condition as testified to by the plaintiff would be correct?

MR. DELANA: That is not true. That statement is not right, the statement that he is going to disregard it.

THE COURT: He has answered the question, and I believe has explained his answer.

MR. GRIFFIN: At this time we object to any opinion of this witness on the ground that he has testified he is going to disregard an important part of plaintiff's evidence, which is plaintiff's exhibit No. 8, which has been put in by plaintiff himself, and is a part of the plaintiff's case; that he will have to disregard that, and that he will weigh the testimony, which is not proper for an expert witness.

(EXAMINATION BY MR. DELANA)

Q. When you were first asked, Doctor, about this you stated that you considered both. Are you going to consider all the evidence of the plaintiff, that is, what the plaintiff said and also the record that is here?

MR. GRIFFIN: Objected to as leading and suggestive.

THE COURT: Overruled.

Q. Are you going to consider this, together with all the rest of the testimony?

A. Yes.

Q. You are going to weigh all of the evidence in giving this opinion?

MR. GRIFFIN: Objected to as leading, if the Court please.

THE COURT: Sustained.

Q. You may state whether you are going to weigh all

of the evidence given to you in the hypothetical question.

A. I am going to weigh all of the evidence given to me.

MR. GRIFFIN: Now, have you come to the conclusion that you are going to disregard it, or regard it, that is, plaintiff's exhibit No. 8.

A. I am going to regard it in my opinion.

MR. GRIFFIN: How much weight are you going to give it compared with the plaintiff's testimony as related in the hypothetical question?

MR. DELANA: Objected to as incompetent, irrelevant and immaterial.

THE COURT: Over-ruled.

MR. GRIFFIN: Which will you give the greater weight, the plaintiff's exhibit No. 8, or the testimony with reference to what occurred at the time of the plaintiff's separation from service?

MR. DELANA: Objected to as repetition, if the Court please.

THE COURT: Well, let him answer again.

A. Which will I give the greater weight?

MR. GRIFFIN: Yes.

A. The plaintiff's testimony, or what else, did you say?

MR. GRIFFIN: Or that which is contained in plaintiff's Exhibit No. 8, in connection with his separation from the service? The question that was asked, "Have you any reason to believe that at the present time you are suffering from any wound, injury or disease, or that you have any disability or impairment of health, whether or not incurred in military service?" and his answer was "No," and the certificate of the examining physician, "That the soldier named above has been given a careful examination and it is found that he had pleurisy, R, on February 14th, 1919," I am asking you now which you are going to give the greater weight? That statement in Plaintiff's Exhibit 8, or the plaintiff's testimony?

A. I will probably give the greater weight to exhibit No. 8.

MR. GRIFFIN: That being the case, we will object to the opinion of the witness on the ground that he is weighing the testimony, which is not the province of an expert witness, and the defendant objects to the question on the ground that the hypothetical question, that it is unintelligible, and that it does not contain a full statement of the evidence, and that as it is related it calls for this witness to pass upon the credibility of the witnesses who have testified in this case, and that such an answer as is called for by the hypothetical question would invade the province of the jury.

THE COURT: Over-ruled.

MR. GRIFFIN: Exception, please.

A. It is my opinion that he was.

(DR. JAMES L. STEWART, a witness called on behalf of the plaintiff, being first duly sworn, testified as follows:)

DIRECT EXAMINATION

Q. You have heard the statement of facts here yesterday, the hypothetical question?

A. Yes, sir.

Q. Assuming the facts as stated yesterday and taking into consideration your examination of Mr. Shaffer in 1932 and again in 1934, and assuming the following definition of total and permanent disability: Total disability is any impairment of mind or body which renders it impossible for the disabled person to follow continuously any substantially gainful occupation, and total disability shall be deemed to be permanent whenever it is founded upon conditions which render it reasonably certain that it will continue throughout the life of the person suffering from it, I will ask you to state whether or not you have an opinion as to whether Mr. Shaffer was totally and permanently disabled at the time of his discharge from the service in 1919, July 1919?

A. Yes, sir.

Q. I will ask you whether in your opinion he was at that time totally and permanently disabled?

MR. GRIFFIN: I object to the question, it was so lengthy as to render it unintelligible and containing conflicting evidence and any opinion rendered by this Doctor would be an invasion of the province of the jury the question calls for the ultimate fact to be decided by the Court and Jury.

THE COURT: Overruled.

MR. GRIFFIN: Exception.

A. I think he was totally and permanently disabled at that time.

(DR. ALFRED BUDGE, a witness called on behalf of the plaintiff, being first duly sworn testified as follows:)

DIRECT EXAMINATION

Q. You heard the hypothetical question in this case.

A. Yes, sir.

Q. Assuming the facts as stated in that question and assuming the following definition of total and permanent disability: Total disability is that condition of mind or body which renders it impossible for the disabled person to follow continuously any substantially gainful occupation, and total disability shall be deemed to be permanent whenever it is founded upon conditions which render it reasonably certain that it will continue throughout the life of the person suffering from it, I will ask you to state whether or not you have an opinion as to

whether Mr. Shaffer was totally and permanently disabled on the 18th day of July, 1919, the date of his discharge.

A. Yes, sir.

Q. I will ask you whether in your opinion he was at that time totally and permanently disabled.

MR. GRIFFIN: Objected to as leading and suggestive and calls for an opinion which is an invasion of the province of the jury.

Q. I will ask you whether or not in your opinion he was totally and permanently disabled at the time of his severance from the United States Army in July, 1919.

MR. GRIFFIN: Objected to on the ground that it calls for an opinion involving the whole merits of the case and invading the province of the jury.

THE COURT: Overruled.

MR. GRIFFIN: Exception.

A. It is my opinion that he was.

On the return of the verdict, in open court, the defendant asked and was granted sixty days in which to prepare, serve and file proposed bill of exceptions. Oct. 5, 1934.

(Title of Court and Cause.)

ORDER EXTENDING TIME FOR FILING BILL
OF EXCEPTIONS AND EXTENDING TERM

Filed Dec. 3, 1934.

Upon application of counsel for the defendant, and good cause shown,

IT IS ORDERED that the defendant have to and including the 15th day of January, A. D., 1935, in which to prepare, serve, and file Bill of Exceptions in the above entitled cause, and

IT IS FURTHER ORDERED that the September term, 1934, of this Court be, and the same hereby is, extended for a period of 64 days from this date for all purposes in respect to the preparing, submitting, lodging and settlement of said Bill of Exceptions.

DATED at Boise, Idaho, this 3rd day of December, 1934.

S/ CHARLES C. CAVANAH,
DISTRICT JUDGE.

(Title of Court and Cause.)

ORDER EXTENDING TIME FOR FILING BILL
OF EXCEPTIONS AND EXTENDING TERM

Filed Jan. 15, 1935.

Upon application of counsel for the defendant, and good cause shown,

IT IS ORDERED that the defendant have to and including the 1st day of March, A. D. 1935, in which to prepare, serve and file Bill of Exceptions in the above entitled cause, and

IT IS FURTHER ORDERED that the September term, 1934 of this court be, and the same hereby is, extended for a period of 75 days from this date for all purposes in respect to the preparing, submitting, lodging and settlement of said Bill of Exceptions.

Dated at Boise, Idaho, this 15th day of January, A. D. 1935.

S/ CHARLES C. CAVANAH,
DISTRICT JUDGE.

(Title of Court and Cause.)

ORDER EXTENDING TIME FOR FILING BILL
OF EXCEPTIONS

Filed Feb. 26, 1935.

Upon application of counsel for the defendant, and
good cause shown,

IT IS ORDERED that the defendant have to and in-
cluding the 27th day of March, A. D., 1935, in which
to prepare, serve, and file Bill of Exceptions in the above
entitled cause.

DATED at Boise, Idaho, this 26th day of February,
1935.

S/ CHARLES C. CAVANAH,
DISTRICT JUDGE.

(Title of Court and Cause.)

ORDER EXTENDING TIME FOR FILING BILL
OF EXCEPTIONS AND EXTENDING TERM

Filed Mar. 25, 1935.

Upon application of counsel for the defendant, and
good cause shown,

IT IS ORDERED that the defendant have to and
including the 1st day of May, A. D., 1935, in which

to prepare, serve, lodge, settle and file Bill of Exceptions in the above entitled cause, and

IT IS FURTHER ORDERED that the September term, 1934, of this court be, and the same hereby is, extended to the 1st day of June, 1935, for all purposes in respect to the preparing, submitting, lodging and settlement of said Bill of Exceptions.

DATED this 25th day of March, A. D., 1935.

S/ CHARLES C. CAVANAH,
DISTRICT JUDGE.

(Title of Court and Cause)

STIPULATION FOR SETTLEMENT OF BILL OF EXCEPTIONS

IT IS HEREBY STIPULATED AND AGREED by and between the respective parties to this action as follows,

a. That the appellant hereby expressly waives its Assignments of Error numbered 4 and 5.

b. That the appellee hereby expressly confesses error in respect of Assignments of Error numbered 1, 2, 3 and 6 and consents that a judgment entered herein in the Court below may be reversed and that this cause may be remanded for retrial pursuant to law and the practice of the Appellate Court.

c. That this cause may be reversed and remanded without notice to either party and without the appearance of either party either by way of brief or person.

d. That the foregoing Bill of Exceptions has been examined by the respective parties hereto and contains all of the evidence adduced at the trial of this cause as may be necessary to present clearly the questions of law involved in the rulings to which exceptions are reserved and which are presented by the Assignment of Errors herein and all of the evidence presented to the jury bearing upon the questions involved in the Assignment of Errors reserved, and that the same may be settled as defendant's Bill of Exceptions and that the judge of this court may sign the hereto attached certificate settling the said Bill of Exceptions.

DATED this 4th day of April, A. D., 1935.

BENTON F. DELANA,

ELBERT S. DELANA,

Attorneys for Plaintiff.

J. A. CARVER,

United States Attorney
for the District of Idaho.

E. H. CASTERLIN,

Assistant United States Attorney
for the District of Idaho.

FRANK GRIFFIN,

Assistant United States Attorney
for the District of Idaho.

A. L. FREEHAFFER,

Attorney for the Department of
Justice.

Attorneys for Defendant.

(Title of Court and Cause)

CERTIFICATE OF JUDGE TO BILL OF
EXCEPTIONS

United States of America,)
District of Idaho,) ss
Southern Division,)

I, CHARLES C. CAVANAH, United States District Judge for the District of Idaho, and the Judge before whom the above entitled action was tried, to-wit,—the cause entitled Dewey M. Shaffer, Plaintiff, vs. United States of America, Defendant, which is No. 1677 of the Southern Division of said District Court,

DO HEREBY CERTIFY that the matters and proceedings embodied in the foregoing Bill of Exceptions are matters and proceedings occurring in the trial of said cause and the same are hereby made a part of the record herein; that the above and foregoing Bill of Exceptions contains all material facts, matters and proceedings heretofore occurring in said cause and not already a part of the record herein, which are necessary to pre-

sent clearly the questions of law involved in the rulings to which exceptions are taken and reserved and presented by the Assignment of Errors, and which is all of the evidence presented to the jury bearing upon the questions involved in the Assignment of Errors as amended by the Stipulation herein, and is a true Bill of Exceptions as to said questions of law; that the above and foregoing Bill of Exceptions was duly, regularly and timely filed with the Clerk of this Court and duly, regularly and timely served, settled and filed herein within the time allowed by law and the rules of this Court; that no amendments were proposed to said Bill of Exceptions excepting the same are embodied herein; that due, regular and timely notice of the time of settlement and certifying said Bill of Exceptions was given and that the same was settled, certified and filed during the trial term of this Court as extended for that purpose.

DATED at Boise, Idaho, this 10th day of April, A. D., 1935.

CHARLES C. CAVANAH.

District Judge.

(Title of Court and Cause)

PETITION FOR APPEAL

Filed Jan. 3, 1935.

COMES NOW the above named defendant, United

States of America, and says that on or about the 6th day of October, 1934, this Court entered judgment upon verdict of the jury in the trial of the above entitled cause against said defendant, in which judgment and proceedings had hereunto in this cause certain errors were committed to the prejudice of the defendant, all of which errors will appear more in detail from the assignment of errors, which is filed with this petition.

And the petitioner further says that said cause was brought against said defendant under Title 38, Section 445, U. S. C. A.; that this appeal is sought and brought up by direction of a department of the government of the United States, to wit, the Department of Justice, and the said defendant in petition herein is acting under the direction aforesaid, and no bond for costs, supersedeas or otherwise ought, pursuant to Sections 869, 870, Title 28, United States Code, be taken or required.

WHEREFORE, the said defendant prays that an appeal be allowed in its behalf in the United States Circuit Court of Appeals for the Ninth Circuit of the United States for the correction of the errors so complained of; that said allowance operate as a supersedeas and no bond therefor or for costs or otherwise be required and that a transcript of the record, proceedings and papers in said cause, duly authenticated, may be sent to said Circuit Court of Appeals, and that citation issue as provided by law.

J. A. CARVER,

United States Attorney for the District of Idaho.

E. H. CASTERLIN

Assistant U. S. Attorney
for the District of Idaho.

FRANK GRIFFIN,

Assistant U. S. Attorney for the District of Idaho.

A. L. FREEHAFFER,

Attorney for the Department of Justice.

(Title of Court and Cause)

ASSIGNMENT OF ERRORS

Filed Jan. 3, 1935.

COMES NOW the defendant in the above entitled cause and files the following assignment of errors upon which it will rely upon the prosecution of the appeal of the above-entitled cause, from the judgment made by this honorable Court on the 6th day of October, 1934.

I.

The Court erred in overruling defendant's objection to the hypothetical question propounded to Dr. O. F. Swindell as follows, to-wit:

“Q. Now, then, will each of you doctors listen to this question I am about to ask here. Each one of you doctors may assume the following facts: That Dewey Shaffer enlisted in Company B, Second Idaho, on April 15th, 1917; that he went overseas on December 24th, 1917; that he debarked at Liverpool, England, and went to LeHavre, France; in January, 1918, he landed at Camp Dijon, France; that along in March, 1918, he took quite a severe cold and had a cough; that he had a running of the ear, that he was confined to quarters for a period of from two to three weeks; that after being confined to quarters for two or three weeks he was placed on light duty consisting of taking dishes and victuals to the ‘mumps’ camp, where some boys were confined with the mumps; that he was placed on regular duty drilling heavy artillery until July 14th, about that time; that during this time Mr. Shaffer coughed continuously, that he had some difficulty in breathing; that on July 14th he contracted a heavier cold than the one he had before, and was placed in a hospital and spent four days there; that during that time he had night sweats and his cough was more severe; that he was returned, not to duty, but to light duty, the light duty consisting of helping the cook in the kitchen and waiting on table, and washing dishes; that after he was returned to light duty, he noticed himself and his fellow companions noticed that he had a cough and that his cough increased, and that his breathing was difficult, and that a part of

the time he was not able to be on light duty; that through July and August the weather was pleasant and they were at the Chateau-Thierry on the front, and that he went to the Meuse-Argonne, the St. Mihiel front, and from August the weather was very sloppy and wet underfoot, and they wore rubber boots and big hob-nailed shoes, that they camped out in the open and laid on the ground, that it became foggy and the weather became colder and disagreeable; that he had night sweats throughout this time, and that one of his buddies said that he had night sweats and his breathing was difficult, and several of the other boys with him said the same thing; that they would come in at night and go to the kitchen where he was supposed to be waiting, and that some of the time he would be in bed and not get up, that he was coughing and wheezing, and that his buddies would go in and see if there was anything they could do for him; that his cough increased, and the difficulty in breathing increased, and that at Armistice time he was placed in his billet, and that his cough increased up until about December 2nd, and his hard breathing increased. On December 2nd they started for France and traveled in trucks,—

“THE COURT: What do you mean when you say ‘they started for France?’

“MR. DELANA: I beg your pardon. I should say they started from France and into Germany, and that all except two or three nights they stayed in the open

and that it was snowing and raining and sleeting, and that Mr. Shaffer's cough became worse, and his breathing more difficult; that about December 22nd, about three days before Christmas, he was taken off light duty and had missed a number of days; that he was finally taken off entirely and was confined to his quarters; that on December 22nd, 1918, this happened, and that he remained on light duty, and while he so remained his cough increased and his hard breathing increased; that on February 14th, 1918 when he was placed in the hospital, and he remained in this hospital from February 14th until some time in April, and that at the time of entry to the hospital he had a temperature of 101 in the morning, and an afternoon temperature of about 103; that the admission to the hospital occurred on February 14th, 1919, as shown by the admission card; that under date of February 14th, 1919, the diagnosis is: Pleurisy, serofibrinous. On February 15th the service records show, lower lung, lower and middle lobe of right lung show numerous rales and increase in vocal fremitus; under February 20th the record shows the diagnosis of increased vocal fremitus and subcrepitant rales in right lower; February 24th shows by a lung examination flatness over right base, posterior, and the breath sounds about the same area, temperature 102; on February 25th the chest was tapped in the sixth interspace and midaxillary line and 100 c.c. of clear yellow fluid withdrawn; and later on March 8th it shows a few moist

rales in the right lower lung. Sheet 2 of this clinical record shows pleurisy, serofibrinous, with tachycardia; on March 20th, roughened breath sounds over the entire left chest, and no rales, left chest shows marked increase in vocal fremitus over right upper, absent breath sounds and diminished fremitus right lower; on March 23rd, pleurisy continues hard; March 26th the same, vocal fremitus still exaggerated in right upper, with exaggerated breath sounds on left, diminished fremitus over right lower, pulse continues high; April 3rd, developed, —I can't read that words, but the next is angina; April 15th, patient very anemic. You may assume that when he got to New York,—By the way, he was taken to France and landed in Brest and was kept in a hospital for a week or ten days, and then he was brought in a hospital ship to New York, and placed in a hospital and diagnosed in New York on May 30th as pleurisy, with effusion; he was brought from New York to Salt Lake City in a hospital train with nurses, and while in the service it is testified that along in March one of his buddies went to visit him and he was very thin and emaciated, and very poor, he was so listless that he didn't carry on any conversation, and one of his buddies went to visit him while he was in the kitchen and he passed him within five feet, and didn't know him, and one of his buddies who knew him as a boy testified that he was in such a condition that he didn't recognize him within about five feet of him; another buddy went to visit him

and he walked with him, and when he was walking three blocks sat down twice to rest, and he walked as if he was very weak, and he didn't recognize him until he walked up within a half block of him; that he then took him and placed him on a billet and gave him a can to spit in, that he was weak and emaciated; that he was visited by his folks while he was in Salt Lake City on about July 4th, 1919, and while there at Fort Douglas in Salt Lake City he kept asking his doctor to get out of the service, telling him that he wanted to be discharged, and his folks left him there, and he kept on asking for his discharge from service, and the doctor told him that he was not ready to release him, but finally on July 18th, 1919, he was discharged from service, and the manner of discharge was that he was sent down with fifteen or twenty other fellows, and they went to a room and he was presented with some blanks, some papers, for his signature, and he signed them; that they were not read to him; that he was not examined by a doctor at the time of discharge; and further that about the date of his discharge he was presented with a typewritten or printed blank whereon this question appears: 'Have you any reason to believe that at the present time you are suffering from the effect of any wound, injury or disease, or that you have any disability or impairment of health, whether or not incurred in the military service?' and the typewritten answer appears: 'No.' And on the same date his superior officer made a certificate which

reads, 'I certify that the soldier named above has this day been given a careful physical examination, and that it is found that he is physically and mentally sound.' You may assume further that immediately following his discharge from the service he returned home; that he got off the train or car and walked about a mile home, and his sister went to meet him and didn't recognize him because of his paleness, weakness, and change in his condition; that that night he slept with his brother, and that he kept his brother awake by coughing and wheezing, and the next night his bed was changed and he was placed on the front porch, and thereafter his sister and his father and brother slept in rooms that were away,—they were the second rooms from him, and they heard him coughing and wheezing; that about the same night of the day after he got home he went to a doctor at Middleton, Doctor Hammer,—Doctor Hammer is not able to testify at this hearing,—and within two weeks after his discharge he went to Doctor Gue, and he told him to go to the mountains; that Doctor Gue had taken some X-rays, and that he, Mr. Shaffer, had made an attempt to get the X-rays but was not able to. That he went to the mountains and his chest pained him more, and his cough was worse, and that he came back within a couple of days; that he came back to Boise and went to Doctor Tolman; that he went there and was given a physical examination, a sputum examination and an X-ray was taken; that Doctor Tolman also punctured his lung and

took from him a cup to a cup and a half of yellow fluid; that Doctor Tolman testified that he had diminished breath sounds, positive sputum, limited motion of the chest, and that the X-ray and the entire examination had shown that he was moderately advanced with a tubercular condition, active condition, that Doctor Tolman treated him for about six weeks, and that he stayed at home the rest of the fall and winter, and went to bed in the mornings, and generally again in the afternoons; that he just laid around and didn't do anything; that his cough continued and his hard breathing continued, and that he bothered his folks and kept them awake some of the night, and along in the spring of 1920 that he leased a part of his father's place,—you may assume, first, that during the fall that he didn't play around with his boy friends; some of his boy friends told about their going swimming, and his having trouble walking about half a mile, and he didn't go in swimming with the other boys. During the fall in playing games there since he had come home, he didn't play in any of the games but just watched them, and didn't participate. He leased his father's place, or a portion of it, but his father put in most of the crops; that Mr. Shaffer stayed in bed most of the time and his cough continued, and his hard breathing also continued, and his father and the rest of the family helped him during that year; that about June, 1920, his brother-in-law came over and stayed with him, and did most of the work on the place, Dewey went out to help run a binder but all that he did in assist-

ing in the cutting of the grain was to bring the horses, and to relieve his brother-in-law at mealtime; and that he did some shocking of grain in the evenings for a couple of hours, and that while he was doing this shocking he had a coughing spell, and that his brother helped him to the house; he didn't help with the threshing except that he was kind of the supervisor, but did not do any of the work, and stayed in the house most of the time; that during September his brother-in-law had a job loading gravel, and Mr. Shaffer attended to the trap on the gravel pit; the gravel was loaded from a trap door and Dewey's job was to scrape the loose gravel into the truck, and also to keep track of the number of loads that were taken out; he was able to do this work for about half of the time that he was there; while he was there working he had a bunk on which he could rest, and he rested probably about half of the time; that one time his father came to visit with him and he was weak and emaciated and looked tired, and his father volunteered to relieve him, and did relieve him that day; that in the winter of 1920 and '21 he stayed at home and didn't do anything; that is, he didn't do anything a great deal of the time but just stay around the house lying down on the cot or on the bed; that in the spring of 1921 he was married and rented a ranch near Kuna; that he went out and endeavored to plow and was seized with a pain in the chest and with coughing and this hard breathing which continued; he went to the house

and he was relieved there at this job of plowing by his brother and some hired help, and he did none of the harrowing of the ground, but when it was ready for the grain he went out and tried to drill, and while drilling he was seized with a coughing and wheezing spell, and his wife went out and relieved him and did the rest of the drilling, and that he endeavored to run a mowing machine during the time they were putting up hay, and was seized with a coughing spell and didn't mow any more of the hay; that during the haying he endeavored to pitch hay on the loads and became exhausted, and then he went to the haystack and tried to handle the fork there, and that he did that until shortly afternoon when he was seized with a coughing and wheezing spell, and he went to bed for the rest of the afternoon; that at the time the grain was harvested it was done with a combine harvester and the people that did this harvesting with this combine, to pay for it and the help, took all of the grain except nine sacks; that the crop was put in by his brother-in-law, and other relatives as I have stated; on July 24th, 1921, he went to his brother-in-law's place, where they were going to get together and go to a Fourth of July celebration, that he got there in the evening and was feeling fairly well, that in the morning he was seized with a coughing and wheezing spell, and they took him on a cot to the celebration and that he laid on the cot most of the day at the celebration; that in the fall of 1921 he went with his wife to pick

prunes; that he went out about seven o'clock in the morning when the rest of them went out, and that he was seized with a coughing spell, and that after that day he didn't go out until after the dew was off; that while he was working at this prune picking the climbing of the ladder and the reaching up for the prunes would bring on these coughing and wheezing spells and he would have to go to the tent and sit down and rest; that during the day this would occur several times; that he went to Doctor Gue again for treatment; that during the latter part of September he went down to Fruitland and got a job trucking, but that he couldn't do this, and then they gave him a job as janitor, picking up the loose boxes, broken boxes and pieces and sweeping out, and that the sweeping would cause a lot of dust and it would bring on these coughing and wheezing spells, and his wife would do the sweeping for him. About the middle of October he went to Payette and got a job in a restaurant washing dishes, but that the heat and the steam there caused this coughing and wheezing, and that during the winter of 1921 and 1922 he and his wife ran a cream station in Payette, and that consisted of taking cream in big cans, but they would have to wash the cream cans and the powder they used in cleaning the cans caused him to cough and to wheeze. His wife did the washing of the utensils. That they had to test the cream, and in making this test they used acid, and that this acid caused him to cough and wheeze, and his wife

would do the testing of the cream, and also his wife opened up the cream station in the morning, and that he didn't come until all the way from nine o'clock until noon, that he was in bed a good deal of the time, and was sick a good portion of the time; that they kept this station until July, 1922, and that he then went to Glenns Ferry and got a job as hostler's helper, and that job was getting up and down on the engine and loading coal and water, and throwing switches for the engineer, and in doing that it would bring on these hard coughing spells and he lost about ten days of the time he was there, and that during that time he lost considerable weight; that he did nothing further until September, and at that time he applied for vocational training, and at about the same time he was examined by Doctor Budge; he was given a complete physical examination, his chest was percussed, and examination was made by stethoscope, examination of the sputum, and the examination of the sputum showed that it contained tubercle bacilli, and the diagnosis was that he was suffering from active tuberculosis and bronchial asthma; that he then started to school in September, and that he missed some days and half days; that he came home early in the afternoon and that he was attended by Doctor Budge, and that at that time he was taking for this asthma hypodermics; that before Christmas of 1922 he had a severe attack of choking and wheezing, and that Doctor Ensign of the Veterans Bureau, and later Doctor Budge was called

and gave him a hypodermic, which gave him some relief; that he continued in school until 1923, that he was sent to the University at Seattle, Washington, with the Government, and that his condition there was worse, his cough was severe, and he missed more school, and his sister testified that when he came home he was so weak that he couldn't walk upstairs, and he had night sweats, and that his pajamas and bedding were wet; and his service record shows that he had night sweats while he was in the service, and his buddies have testified that he also had night sweats while he was in the service, and his sister testified that immediately after he got home he had night sweats, and that it was necessary to change the bed because the bedding would be wet. That he stayed in school and missed some time, until March, 1923, when he was taken to a private hospital in Seattle; that he was confined in that hospital about ten days, and then he was taken to Portland to the Veterans Hospital and remained there until about July 10th of that year; that he was by the doctors at that time sent out camping; that he went back to Seattle and got his camp equipment and on the way he was seized with a wheezing and coughing spell, and on arriving at Seattle he was weak, and all that night he was unable to sleep until toward morning and then he was allowed to sleep until noon the next day; that he left Seattle and went out on this camping trip at or near the Dalles, Oregon, and he was to be gone for a period of about three weeks, but that he went back

to Portland in a couple of days; that he was released from the Portland Hospital with the advice to go to a drier climate, and that they went to Long Beach, California, taking fifteen days to make the trip, because they were driving slow on account of his condition, and he was not able to go very far at a time, he was weak and emaciated; that they got to California and rented an apartment and the next day he was asked to move on account of the disturbance of the other guests by his coughing and wheezing; that along in September, 1923, he was visited by one of his ex-servicemen who testified that he had a very severe coughing spell, and that he burned some kind of stuff and inhaled it, and it seemed to relieve him; that he got a job with a newspaper and had a crew of men or boys under him, and that he would take the crew out and while they were working he would rest, if he wanted to, and that he continued to oversee this crew for about five weeks; that he then got a job with a real estate firm and made two sales and earned \$45.00 in about five weeks; that in December, 1923, he applied for vocational training and was given vocational training, continuing with bookkeeping; that he continued until September, 1924, and that he and his brother and his wife testified that he was out of school days and parts of days at a time, that he would come early in the afternoon, and that he had a great deal of difficulty at night in breathing, and with his coughing, that he would get up and walk around sometimes,

and that sometimes at night he would get up and he and his wife would ride out in the hills as the air seemed to give him relief; that the doctor would give him hypodermics, and that in December, 1923, to September, 1924, he went,—that in December, about Christmas time, it was Doctor Morongie who gave him the hypodermic to relieve him, and that between December, 1923, and September, 1924, he would take hypos as high as twenty-five or thirty times; that in September, 1924, the Government changed him from bookkeeping in this vocational training to electrical fixtures, to a repair man's work, and that he was with one firm for about three weeks and that during that time he missed a good deal of time; that he went to Doctor Morongie, that he was coughing and wheezing more, and that while he was doing this work he went out riding more often at night; that he worked for the Hale Electric Company for forty-seven days, and that after he had been working there for about six days he was seized with a violent coughing and wheezing spell and went home, and was there for about ten days; that he went back to work again and had another spell and was carried out by one of his fellow workers; that he then from the Hale Electric Company to the Wilkerson Shop Company and took the same kind of training; that his wife testified on arriving home at night he would go to Doctor Morondie as high as sixty times in that year, and Doctor Morondie testified that he examined his chest, percussed, examined

it with a stethoscope and took a sputum test, and testified that the sputum was positive tubercular, that he had a temperature, and that his pulse was high, that he had a wheeze, and that he had to relieve him by giving him a hypodermic; that he treated him during the two years while he was taking vocational training, and on an average of every ten days and sometimes oftener, and sometimes less, and in the fall he was taking training and that he got worse; he and his wife then got a house in Alcadena and he quit vocational training and later came back to Eagle, Idaho, and that he was examined in 1925 by Doctor Smith and Doctor West, and that Doctor Smith testified that he was suffering at that time from tuberculosis and asthma, that he had a temperature and that his pulse was high, and that there was a limitation of the chest movement; that at about the same time he went to Doctor Budge and upon an examination of him by Doctor Budge who testified that he was suffering from active tuberculosis and that both lungs showed diminished breath sounds; that he stayed out home with his parents that winter and did nothing, and that in the spring of 1926 he rented the Ryles place east of Middleton, that in the spring he went out to plow and was seized with a coughing spell, and at one time his sister relieved him, and at another time his brother relieved him, and that in the drilling of the grain he did the drilling by working for two or three hours a day, that in the irrigating time he didn't do much of that, but that

at one time he was irrigating and he was seized with a coughing spell and one of his neighbor's boys came along and put him in his car and took him home; that in the haying time he went out with his father to pitch hay and he was seized with a coughing spell, and he got one of his neighbors to take him to his place and he rested the rest of the day, and in pitching he would pitch on the bottom of the wagon until it got up high, and then the other two of them put on the rest, and he would sit around in the shade and rest; in threshing time he did nothing except manage the crew, and during the cutting of the grain his brother ran the binder and he didn't do any shocking, but at threshing time he did nothing, except as I say, to manage the crew, that is, by the way of working. His neighbor had a thresher and he got a job hauling grain for a man by the name of Spillman, and his job was to haul the grain from the thresher to Middleton and unload it; he endeavored to handle it but it brought on coughing spells and he was unable to do that; that he has some clover to cut in a field and he went out at four o'clock in the morning and cut until the dew was off, and he got along fairly well the first morning, and that the other days he didn't get along; that in shocking the clover he went out the first morning,—or, rather, the second morning, after he was out about half an hour he was seized with this coughing and wheezing spell and the rest of the time he did nothing, he didn't go back at this and did not do anything the

balance of the fall; that in September he took a series of eight treatments from Doctor Elbert of Caldwell, and that same summer he went out with his brother to run a dyking machine, and this was dusty and he was unable to do this, and he hired one of the neighbors to come in and relieve him, and he went to the house; in 1927, as to his farming operations he testified he had to hire a lot of help and his expense was high, that the income was about \$125.00 in his favor,—that was not including the depreciation of his car and the running expense and the living expense of himself and wife; in January, 1927, he ran the same place,—that is, in 1927, I should say, he ran the same place again, the Ryles place, for the second year, and he went out to plow and fence and tried to harrow, and was unable to do so; he was seized with coughing spells and went to the house; he didn't do any plowing or harrowing; in harvest time he went out to relieve the regular man during the meal times; he didn't shock any grain at all, and during the threshing time he didn't do anything except just boss the job, and during the threshing he was seized with a very severe coughing and wheezing spell, and his brother and a neighbor boy helped him to the house, and he was not able to walk at that time without their help; he was forced to stop two or three times on the way, as these people testified that he had a hemorrhage, and that he raised about a cup or a cup and a half of blood on the way to the house; that he had a coughing spell that night, and they were

afraid they were going to lose him; Doctor Budge was called about five o'clock in the morning, and he came and administered a hypo; the next night he had a severe spell again and became unconscious; that his father and brother took him riding at night and in the early morning to get relief from these severe spells of coughing and wheezing, and that he was taken to Doctor Pittinger at Boise and thereafter for about a week they would go out riding at night to get relief from these severe spells; in July 1927 he applied for reinstatement of \$3,000 of the \$10,000 insurance policy; on the first page the question is asked: 'Are you disabled on account of any injury or disease?' and the typewritten answer was, 'Yes.' And in asking on the following page whether or not he was totally and permanently disabled, the answer was written in, 'No,' and the explanation is that at the time he came out of the service up to 1927 he did not know that war risk insurance covered disability, and that he didn't know it until 1929 when he went to the hospital here, to the Veterans Hospital, and was told by Doctor Stallings; he testified the only disability he knew anything about was compensation disability; that he gave his history as having had treatment by Doctor Tolman for his lungs, by Doctor Gue for his lungs, Doctor Smith for his lungs, Doctor Morondie for his lungs, and these were in 1920, 1926, 1924 and 1925, and in answer to the doctor's questions he answered that he was treated in 1919 and 1920 for lungs, and also in hospital No. 77 in Portland, Ore.

gon; that in August, 1927, he went to Doctor Boeck in Boise, and Doctor Boeck gave him a series of twenty-four treatments, that he had these treatments and that at the time he gave him these twenty-four treatments that he didn't get better and he advised him to change climate; Doctor Boeck said he was wheezing so badly that you could hear him for quite a distance; that he went to Yakima, he and his wife, got a job there in an apple warehouse, and he was there for about four weeks, and he worked twelve days out of the four weeks; he went to Doctor Middleton at Yakima, and he was given a course of treatments for asthma, taking adrenalin as high as twelve times at night; he left Washington and went to Portersville and then he went to Lindsay. This job he had in the warehouse at Yakima trucking apples, or fruit, brought on a severe coughing and wheezing spell, and he was then given a job scattering papers around for the boxes, the fruit boxes, and this is a job that a school boy did before him; that he was taking as high as 15 hypodermics of adrenalin during a night; he went to California and he rested there during the winter and about February 1st he leased a service station and sold oil and gas and accessories, and he got along fairly well for about two weeks, but he had the same inability to sleep, and his wife opened up the station in the morning and he would come all the way from nine o'clock until twelve, and they had a mechanic there to help with the work; his wife testified that there was

about a third of the time that he was seized with these coughing spells, and sometimes was carried out, and that at one time he was taken to the Community Hospital, and there he was given some treatment by being given hypos; that he stayed there about half a day and then his wife and some friends took him home, and he had to be helped into the house; that along in April, 1928, he took about thirty hypos from Doctor Arlett, and that his condition was about the same, and he came back to Eagle, and he was treated by Doctor Budge for asthma, and that about September 1st, 1928, he went to Washington, to Cashmere, Washington, and got a job as foreman in an orchard, and his duties there were to look after the pickers, and his testimony is that he worked perhaps a half, or a little more than half of the time while he was there, and the rest of the time he was in the tent resting, and upon going to the tent at noon or in the evening his wife or brother would find him lying down, he was taking adrenalin for relief practically every night; that he went back to California about October 1st, and got the same job that he had before, that is, distributing papers to the packers of this fruit to line the boxes with, that this took him three or four hours a day, and that he came back to Eagle after that about Christmas time in 1928, and stayed until March of 1929; that his condition got worse and he had more night sweats, more trouble at nights, and in March, 1929, he was treated by Doctor Budge for his trouble, and at that

time he had a temperature; in March, 1929, he left and went to Arizona. The testimony is the first day they traveled about a hundred miles, and they took about fifteen days or two weeks to make the trip, traveling very slowly because of his weakened condition. They stayed there for about five weeks, and he got worse, and then he went from there to Ely, Nevada, and got a job for about two weeks as clerk in a hotel, and that he was taking adrenalin all of the time and taking it on the job as clerk at the hotel; that he was having trouble and was taking this adrenalin when the boss caught him taking it one evening and he was discharged; that they got a room in an apartment house there and the landlady complained of his disturbing the other people, and they were required to move out; that they came in July, 1929, back and he went into the Veterans Hospital June 30th,—or rather on June 15th, 1930, and was doctored at that time in the Veterans Hospital and was confined to bed in the ward there taking tubercular treatment, rest in the morning and afternoon, and on getting out of the hospital he went to the mountains for his health. After he had been there for a short time he endeavored to help a sheepherder to butcher a sheep and it brought on a severe coughing spell and wheezing spell, and he was in bed for three or four days. Then he made a trip to Loon Lake, which was about five miles, and it took him six hours to make the trip, and he was there a short time when he got a sore throat and had pains in his chest,

when he came back to Boise, and the doctor then sent him to the hospital, that is, Doctor Budge after giving a complete examination and taking a test of his sputum, and the sputum was positive, testified he had an active tubercular condition, complicated by pleurisy and asthma. Mr. Shaffer stayed here in Boise until November, 1930, when he left and went to California. He thought that it would be better in California for his health. They took an apartment in Venice but he disturbed the people so much that he was requested to move, and they did move. They moved back to the east side of Los Angeles and lived there until they returned to Boise in February of 1931. During all of this time he was taking adrenalin, all winter. They lived in Boise until August, 1931, and he didn't do any work. A Mr. Wilcox testified that he slept with him in February, 1931, and that he was getting up in the night and taking adrenalin; that his bed was wet with night sweats, and that in August, 1931, he went to visit his folks at threshing time in Eagle, that he wasn't doing any work but being around there the dust of the thresher brought on a coughing spell, and about April 1st, 1932, he went up to Jordan Valley to cook; he was supposed to bring in the wood and the water, and his wife went up there to take this job; he was supposed to bring in the wood and the water, but in chopping the wood and carrying the water it brought on choking and coughing spells, and made him very weak, and in carrying the water it had to be carried

up an incline for about four hundred yards, and that brought on severe coughing spells, and thereafter the other men there carried the water for him; that in washing dishes the steam and the heat would bring on wheezing and coughing spells; that the last severe coughing spell he had, one of the boys went to get a car to take Mr. Shaffer to Jordan, and that during the time he was gone for the car Mr. Shaffer was taking adrenalin, and that when he came back they took him to Jordan Valley, and they had to stop for him to take his adrenalin because of the severe coughing spells; that in March 1932 an X-ray was taken at St. Luke's, and according to the testimony of Dr. Stewart it showed tuberculosis in both lungs; that about May 1st, 1932, Mr. Shaffer moved to Caldwell, Idaho, and that moving from one place to another there they had only personal effects to move, and he would have to make three or four trips in order to move them; that he had to move from one place to another because he was up in the night, coughing, and he disturbed the other people and they were requested to move, and that Mr. Wilcox testified that he and his brother and Mr. Shaffer were going on the Fourth of July on a camping trip up on Shaffer Creek, that they were to stay three or four days, that he was up all night the first night,—about all night,—coughing and wheezing, and he went to bed about sun-up in the morning and slept until noon, and that that afternoon they loaded up the car and came back home; that the last of July he

went to visit his sister in Seattle, intending to stay about three weeks, that upon getting there he was seized that night with a coughing and wheezing spell, and they were up most of the night and he was taking adrenalin and didn't go to bed until the next morning; that he stayed the next night, and the third morning they left to return home; that he was in bed then about a week or ten days,—or, rather, about ten days or two weeks. Mr. Wilcox testified he was around there for about three weeks, and that he often saw him taking adrenalin, and that he often woke him up; that about January, 1933, the only work he did—he did no work in 1931, and in 1932 the only work he did was in a sheep camp for about a week; in 1933 all he did was to help install some streets at Caldwell for the disabled veterans, and in 1933 he had another severe spell. His temperature was taken at 100 degrees and eight-tenths; that in the latter part of September, or in the month of November he moved to another place in Caldwell, carrying his personal belongings, and that brought on a coughing and wheezing spell, and a man helped them to move. He did no more work in 1933, and in January, 1934, he was seized with a severe coughing spell, and his friend Elbert Hardy testified that he was coughing severely, and that he went to the bathroom and that he could hear him coughing and wheezing from there; that he moved to Boise in March, 1934, and in March, 1934, he got a job with the FERA. His brother would take the horses to the job for him and take them home in the evening, and he would go

home in a car; his job was driving a team, but on this job his coughing and wheezing increased and he worked for two days the first week, and one the next, and two the third. From 1928 up to the present time Doctor Budge has testified that he has been attended by him once or twice a month, that he was suffering with active tuberculosis and pleurisy at the times he was examined; and Doctor Swindell testified that he had active tuberculosis in both lungs, and a sputum examination revealed positive sputum on June 27th, and on July 6th and on July 27th, he had tubercle bacilli. Assuming the above facts, and assuming the definition of total and permanent disability to be, that is, total disability is any impairment of mind or body which renders it impossible for the disabled person to follow continuously any substantially gainful occupation; and total disability shall be deemed to be permanent whenever it is founded upon conditions which render it reasonably certain that it will continue throughout the life of the person suffering from it, now, Doctor, I will ask you, assuming these facts, and taking this definition, whether you have an opinion as to the total and permanent disability of the plaintiff at the time of his discharge from the army on July 18th, 1919.

“A. Yes, sir.

“Q. I will ask you to state whether or not, in your opinion, he was totally and permanently disabled at the time of discharge from the army on July 18th, 1919.

“MR. GRIFFIN: I would like to ask a question.

(Questions by Mr. Griffin):

Doctor, in this hypothetical question it was called to your attention that when the plaintiff separated from the service of the United States that this question was asked: ‘Have you any reason to believe that at the present time you are suffering from the effects of any injury or disease, or that you have any disability or impairment of health, whether or not incurred in the military service?’ and the answer to that is ‘No.’ And the plaintiff explains that by saying he wasn’t asked that question; that there is a certificate here reading, on plaintiff’s exhibit 8, by the commanding officer, ‘I certify that the soldier named above has this day been given a careful physical examination, and it is found that he had pleurisy R on February 14th, 1919,’ and that is signed by William F. Burns,—Burr, I guess it is, Major, M.C.U.S. Army. Plaintiff testified that he did not receive any examination. Now, Doctor, which of these do you believe? Do you believe the testimony in the hypothetical question, or do you assume the record as contained in Plaintiff’s Exhibit 8 as being true?

“THE COURT: He is asking you which of these do you take into consideration when you give this opinion?

“MR. DELANA: He might take both of them together.

“A. You want me to state which one I think are the facts?

“Q. (By Mr. Griffin): Yes.

“A. I think both are the facts. I think the plaintiff's memory is probably at fault, when he said he didn't receive a physical examination.

“Q. (By Mr. Griffin): Do you think that both are true?

“A. I think that both men were telling the truth.

“Q. (By Mr. Griffin) And in your opinion which are you going to give the greater weight to, the evidence contained in plaintiff's exhibit 8, that I have read, or the testimony of the plaintiff that has been read to you in the hypothetical question, in arriving at your opinion?

“A. Regarding this examination?

“Q. (By Mr. Griffin) Yes, regarding that.

“A. I think I could disregard both.

“Q. (By Mr. Griffin) You are going to disregard these?

“A. You mean the fact that he didn't have a physical examination when he was discharged? I would probably give greater weight to your record there of the examination.

“Q. (By Mr. Griffin) To this record in plaintiff's exhibit 8?

“A: I think I am a little confused about the two facts.

“Q. (By Mr. Griffin) It will be necessary in giving your opinion to consider the record as true, or the testimony as true,—you have to say that one or the other,—both cannot be true.

“A. I will give the greater weight to the testimony of the plaintiff.

“Q. (By Mr. Griffin) So you have to disregard plaintiff’s Exhibit No. 8?

“A. What is Exhibit No. 8?

“Q. (By Mr. Griffin) That is what I read to you where it contains that he says there was nothing wrong with him, and also the certificate of the examining officer, that is plaintiff’s Exhibit 8.

“A. I will accept the testimony of the plaintiff.

“Q. (By Mr. Griffin) And disregard the other?

“A. Yes.

“Q. (By Mr. Griffin) Now, Doctor Swindell, when the plaintiff made application for reinstatement of a yearly renewal insurance under date of July 2nd, 1927, in answer to question as to his condition, ‘Are you in good health?’ he answered that he was in fair health. What consideration will you give that in your opinion?

“A. I will regard that, but I have a feeling that the man didn’t realize his physical condition when he made the statement.

“Q. (By Mr. Griffin) You believe that this exhibit, Defendant’s Exhibit No. 9, is wrong, and the condition as testified to by the plaintiff would be correct?”

“MR. DELANA: That is not true. That statement is not right, the statement that he is going to disregard it.

“THE COURT: He has answered the question, and I believe has explained his answer.

“MR. GRIFFIN: At this time we object to any opinion of this witness on the ground that he has testified he is going to disregard an important part of plaintiff’s evidence, which is plaintiff’s exhibit No. 8, which has been put in by plaintiff himself, and is a part of the plaintiff’s case; that he will have to disregard that, and that he will weigh the testimony, which is not proper for an expert witness.

(EXAMINATION BY MR. DELANA)

“Q. When you were first asked, Doctor, about this you stated that you considered both. Are you going to consider all the evidence of the plaintiff, that is, what the plaintiff said and also the record that is here?”

“MR. GRIFFIN: Objected to as leading and suggestive.

“THE COURT: Overruled.

“Q. Are you going to consider this, together with all the rest of the testimony?”

“A. Yes.

“Q. You are going to weigh all of the evidence in giving this opinion?

“MR. GRIFFIN: Objected to as leading, if the Court please.

“THE COURT: Sustained.

“Q. You may state whether you are going to weigh all of the evidence given to you in the hypothetical question.

“A. I am going to weigh all of the evidence given to me.

“MR. GRIFFIN: Now, have you come to the conclusion that you are going to disregard it, or regard it, that is, plaintiff's exhibit No. 8.

“A. I am going to regard it in my opinion.

“MR. GRIFFIN: How much weight are you going to give to it compared with the plaintiff's testimony as related in the hypothetical question?

“MR. DELANA: Objected to as incompetent, irrelevant and immaterial.

“THE COURT: Overruled.

“MR. GRIFFIN: Which will you give the greater weight, the plaintiff's exhibit No. 8, or the testimony with reference to what occurred at the time of the plaintiff's separation from service?

“MR. DELANA: Objected to as repetition, if the Court please.

“THE COURT: Well, let him answer again.

“A. Which will I give the greater weight?

“MR. GRIFFIN: Yes.

A. The plaintiff's testimony, or what else, did you say?

“MR. GRIFFIN: Or that which is contained in plaintiff's Exhibit No. 8, in connection with his separation from the service? The question was asked, ‘Have you any reason to believe that at the present time you are suffering from any wound, injury or disease, or that you have any disability or impairment of health, whether or not incurred in military service?’ and his answer was ‘No,’ and the certificate of the examining physician, ‘That the soldier named above has been given a careful examination and it is found that he had pleurisy, R, on February 14th, 1919,’ I am asking you now which you are going to give the greater weight? That statement in Plaintiff's Exhibit 8, or the plaintiff's testimony?

“A. I will probably give the greater weight to exhibit No. 8.

“MR. GRIFFIN: That being the case, we will object to the opinion of the witness on the ground that he is weighing the testimony, which is not the province of an expert witness, and the defendant objects to the question

on the ground that the hypothetical question, that it is unintelligible, and that it does not contain a full statement of the evidence, and that as it is related it calls for this witness to pass upon the credibility of the witnesses who have testified in this case, and that such an answer as is called for by the hypothetical question would invade the province of the jury.

“THE COURT: Over-ruled.

“MR. GRIFFIN: Exception, please.

“A. It is my opinion that he was.”

II.

The Court erred in denying defendant's objection to the testimony of Dr. James L. Stewart, a witness called on behalf of the plaintiff, which said testimony was as follows:

“Q. You have heard the statement of facts here yesterday, the hypothetical question?

“A. Yes, sir.

“Q. Assuming the facts as stated yesterday and taking into consideration your examination of Mr. Shaffer in 1932 and again in 1934, and assuming the following definition of total and permanent disability: Total disability is any impairment of mind or body which renders it impossible for the disabled person to follow continuously any substantially gainful occupation, and total disability shall be deemed to be permanent whenever it

is founded upon conditions which render it reasonably certain that it will continue throughout the life of the person suffering from it, I will ask you to state whether or not you have an opinion as to whether Mr. Shaffer was totally and permanently disabled at the time of his discharge from the service in 1919, July 1919?

“A. Yes, sir.

“Q. I will ask you whether in your opinion he was at that time totally and permanently disabled?

“MR. GRIFFIN: I object to the question, it was so lengthy as to render it unintelligible and containing conflicting evidence and any opinion rendered by this Doctor would be an invasion of the province of the jury the question calls for the ultimate fact to be decided by the Court and Jury.

“THE COURT: Overruled.

“MR. GRIFFIN: Exception.

“A. I think he was totally and permanently disabled at that time.”

III.

The Court erred in denying defendant's objection to the testimony of Dr. Alfred Budge, a witness called on behalf of the plaintiff, which said testimony was as follows:

“Q. You heard the hypothetical question in this case.

“A. Yes, sir.

“Q. Assuming the facts as stated in that question and assuming the following definition of total and permanent disability: Total disability is that condition of mind or body which renders it impossible for the disabled person to follow continuously any substantially gainful occupation, and total disability shall be deemed to be permanent whenever it is founded upon conditions which render it reasonably certain that it will continue throughout the life of the person suffering from it, I will ask you to state whether or not you have an opinion as to whether Mr. Shaffer was totally and permanently disabled on the 18th day of July, 1919, the date of his discharge.

“A. Yes, sir.

“Q. I will ask you whether in your opinion he was at that time totally and permanently disabled.

“MR. GRIFFIN: Objected to as leading and suggestive and calls for an opinion which is an invasion of the province of the jury.

“Q. I will ask you whether or not in your opinion he was totally and permanently disabled at the time of his severance from the United States Army in July, 1919.

“MR. GRIFFIN: Objected to on the ground that it calls for an opinion involving the whole merits of the case and invading the province of the jury.

“THE COURT: Overruled.

“MR. GRIFFIN: Exception.

“A. It is my opinion that he was.”

IV.

The Court erred in denying defendant's motion for directed verdict made at the conclusion of all the evidence submitted in the case, which said motion was as follows:

“MR. GRIFFIN: If Your Honor please, comes now the defendant at the close of the evidence, the plaintiff and the defendant having rested, and moves the Court to direct a verdict in favor of the defendant and against the plaintiff for the reason and upon the ground that the evidence is insufficient to show or to prove that the plaintiff became totally and permanently disabled within the definition of total and permanent disability in evidence in this case, during the time that the policy of insurance was in full force and effect or at all, and there is no sufficient evidence upon which the Jury can predicate a verdict for the plaintiff and against the defendant in this case.

“THE COURT: The request will be denied.

“MR. GRIFFIN: Exception, please.

“THE COURT: Yes.”

V.

That the evidence is insufficient to support the verdict in that the evidence wholly fails to establish that the

plaintiff was or became permanently and totally disabled while his war risk insurance contract was in full force and effect or at all or at any time whatsoever.

VI.

That the verdict and judgment are contrary to law.

J. A. CARVER,
United States Attorney
for the District of Idaho.

E. H. CASTERLIN,
Assistant United States Attorney
for the District of Idaho.

FRANK GRIFFIN,
Assistant United States Attorney
for the District of Idaho.

A. L. FREEHAFFER,
Attorney, Department of Justice.

(Title of Court and Cause)

ORDER ALLOWING APPEAL

Filed Jan. 3, 1935.

Upon the petition for appeal, accompanied by Assignment of Errors, heretofore filed herein, it being made to appear that said Petition should be allowed and that appeal is sought and brought up by direction of a de-

partment of the government of the United States, to-wit: the Department of Justice,

IT IS ORDERED that said petition for appeal be and hereby is granted and an appeal allowed.

DATED this 3rd day of January, A. D., 1935.

CHARLES C. CAVANAH,
District Judge.

(Title of Court and Cause)

CITATION ON APPEAL

Filed Jan. 3, 1935.

THE PRESIDENT OF THE UNITED STATES
TO DEWEY M. SHAFFER and to DELANA and
DELANA, his attorneys, GREETINGS:

You are hereby cited and admonished to be and appear at the United States Circuit Court of Appeals for the Ninth Circuit to be held at the city of San Francisco in the State of California within thirty days from the date hereof pursuant to Order Allowing Appeal regularly issued, and which is on file in the office of the Clerk of the District Court of the United States for the District of Idaho, Southern Division in action pending in said court wherein the United States of America is appellant and Dewey M. Shaffer is appellee, and to show cause, if any there be, why the judgment and proceedings in said Order mentioned should not be corrected and speedy justice should not be done to the parties in that behalf.

WITNESSETH: The Honorable Charles Evans Hughes, Chief Justice of the Supreme Court of the United States of America, this 3rd day of January, A. D., 1935.

CHARLES C. CAVANAH,
U. S. District Judge.

ATTEST:

W. D. McREYNOLDS, *Clerk.*

(SEAL)

(Title of Court and Cause)

PRAECIPE FOR TRANSCRIPT OF RECORD

Filed Jan. 3, 1935.

To the Clerk of the above entitled court:

Please prepare, certify, print, return and transmit to the Circuit Court of Appeals, Ninth Circuit at San Francisco, California, transcript of record in the above entitled cause, including therein

1. Complaint
 2. Amended Answer
 3. Minutes of the Court
 4. Verdict of the Jury
 5. Judgment
 6. Bill of Exceptions
 7. Petition for Appeal
 8. Assignment of Errors
 9. Order allowing Appeal
 10. Citation on Appeal
 11. Praecipe for transcript of Record
 12. Acceptance of Service of Assignment of Errors, Petition for Appeal, Order Allowing Appeal, Praecipe for Transcript of record, and Citation on Appeal.
 13. Minutes or stipulation and order concerning and settling Bill of Exceptions
- showing in each case fact and date of filing and acceptance of service. Omit printing of title, court and cause and verification.

J. A. CARVER,
United States Attorney for
Dist. of Idaho,
E. H. CASTERLIN,
Assistant U. S. Attorney for
Dist. of Idaho,
FRANK GRIFFIN,
Assistant U. S. Attorney for
Dist. of Idaho,
A. L. FREEHAFFER,
Attorney, Department of Justice.

(Title of Court and Cause.)

ACCEPTANCE OF SERVICE

Filed Jan. 4, 1935.

Service of

ASSIGNMENT OF ERRORS

PETITION FOR APPEAL

ORDER ALLOWING APPEAL

PRAECIPE FOR TRANSCRIPT OF RECORD

CITATION ON APPEAL

is hereby accepted and receipt of copies thereof acknowledged this 4th day of January, A. D., 1935.

DELANA & DELANA,

By BENTON F. DELANA,

Attorneys for Plaintiff.

(Title of Court and Cause.)

CERTIFICATE OF CLERK

I, W. D. McReynolds, Clerk of the District Court of the United States, for the District of Idaho, do hereby certify the foregoing transcript of pages numbered from 1 to 112, inclusive, to be full, true and correct copies of the pleadings and proceedings in the above entitled cause, and the whole thereof, and that the same constitute the transcript of the record herein upon appeal to the United States Circuit Court of Appeals for the Ninth Circuit, as requested by the Praecipe filed herein.

I further certify that the cost of the record herein amounts to the sum of \$139.60, and that the same has been paid by the appellant.

WITNESS My hand and the seal of said Court this 25th day of April, 1935.

(Seal)

W. D. McREYNOLDS,
Clerk.

